

# Private Enforcement of Shareholder Rights

A comparison of selected jurisdictions and policy alternatives for Brazil





# Private enforcement of shareholder rights

A comparison of selected jurisdictions and  
policy alternatives for Brazil



**Please cite this report as:**

OECD (2020), "Private enforcement of shareholder rights: A comparison of selected jurisdictions and policy alternatives for Brazil", <http://www.oecd.org/corporate/shareholder-rights-brazil.htm>.

Photo credits: Cover © antishock/iStock/Getty Images Plus.

© OECD 2020

*This work is published under the responsibility of the Secretary-General of the OECD. The opinions expressed and arguments employed herein do not necessarily reflect the official views of OECD member countries.*

*This document, as well as any data and any map included herein, are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area*

# Foreword

This publication is the output of a joint project involving the OECD, Brazil's Securities and Exchange Commission (*Comissão de Valores Mobiliários* - CVM) and Ministry of Economy to support the strengthening of Brazil's framework for the private enforcement of shareholder rights. With funding from the United Kingdom's Prosperity Fund, the first phase of the project involved the development of an Issues Note and organisation of an experts workshop focusing on private enforcement, held in Brazil on 8-9 November 2018. The research and expert input generated through this project provided the basis for an [Interim Report](#) issued by a CVM/Ministry of Economy Task Force on 2 December 2019. The report identified a number of steps that could be taken to strengthen Brazil's legal framework for private enforcement of shareholder rights, and prioritised two particular areas – the use of derivative suits and collective arbitration – for further research and policy dialogue for a second phase of the project. The underlying objective of both phases of the project is to strengthen Brazil's framework for the enforcement of shareholder rights in alignment with the [G20/OECD Principles of Corporate Governance](#) (“G20/OECD Principles”) and, in particular, the overarching Principle for Chapter 2, which states that “all shareholders should have the opportunity to obtain effective redress for violation of their rights.”

The three research reports that are incorporated in chapters 2 to 4 of this report – prepared by consultants commissioned by the OECD – were discussed at a series of virtual workshop sessions from 22 to 25 June, 2020 with Brazilian stakeholders and a selection of experts from Brazil, Germany, Israel, the United Kingdom, the United States and the OECD Secretariat.

**Chapter 1** provides a brief introduction to and summary of key points from the following chapters and insights from the 2020 workshop, covering (i) relevant goals when designing instruments for the private enforcement of shareholder rights, and (ii) the main features of legal systems that were covered in the two comparative law chapters. It concludes with a set of prioritised recommendations to strengthen Brazil's framework for the private enforcement of shareholder rights.

The recommendations described in Chapter 1 draw upon the analyses in the attached chapters, discussions with the OECD Corporate Governance Committee delegates, and insights from the 2020 workshop. The recommendations are based on analysis of the experience of 10 jurisdictions, while taking into account the specific conditions and requirements to support their effective adaptation to the Brazilian context.

**Chapter 2** compares a selection of nine jurisdictions on frameworks for the use of derivative litigation.

**Chapter 3** compares the same group of jurisdictions plus one additional country on frameworks for the use of corporate and securities arbitration.

**Chapter 4** focuses in greater detail on Brazil's legal and regulatory framework in these areas and, taking account of the other two chapters, proposes possible reforms.

The workshop discussion was helpful in obtaining additional insights into these issues and has been integrated into the development of the four chapters.

The jurisdictions whose frameworks are covered in the comparative chapters include Brazil, France, Germany, Israel, Italy, Portugal, Singapore, Spain, the United States and the United Kingdom. The selection of those countries was based on multiple criteria, including a balance between Civil and Common Law traditions, diversity of regions and the effectiveness of the existing frameworks in some of those jurisdictions.

The Corporate Governance Committee reviewed and approved publication of the report under the responsibility of the OECD Secretary General in November, 2020.

The first chapter of this report has been developed by Caio Figueiredo C. de Oliveira under the supervision of Daniel Blume of the Corporate Governance and Corporate Finance Division of the OECD Directorate for Financial and Enterprise Affairs. All the other chapters were developed by consultants under the supervision of both Caio de Oliveira and Daniel Blume: Martin Gelter authored Chapter 2; Chapter 3 was co-authored by Andre Luis Monteiro and Renato Beneduzi; and Chapter 4 was authored by Guilherme Setoguti J. Pereira. The authors are grateful to CVM Commissioner Gustavo Gonzalez for his active involvement in and support of this project throughout, to the OECD Corporate Governance Committee delegates, Yun Tang (OECD) and all the participants of the 2020 OECD workshop on private enforcement for valuable comments and inputs. Further thanks to Anaísa Gonçalves and Katrina Baker (OECD) for excellent editorial support.

Chapters 2 to 4 contain a number of additional, more detailed proposals for reform. While these detailed recommendations do not necessarily reflect the views of the OECD or its Members, they are offered for the Brazilian Government's consideration as additional possible steps to strengthen Brazil's framework for the private enforcement of shareholder rights.

# Table of contents

Foreword	3
1. Summary of main findings and recommendations	7
1.1. Relevant goals for the private enforcement of shareholder rights	7
1.2. Key points on derivative litigation	7
1.3. Recommendations on derivative litigation	8
1.4. Key points on arbitration	14
1.5. Recommendations on corporate arbitration	16
1.6. Other factors to consider	19
Notes	20
2. Report on derivative litigation	23
2.1. Overview	24
2.2. Derivative litigation systems: Suitable defendants and admissible types of claims	25
2.3. Suits initiated in the shareholder meeting	29
2.4. Suits initiated by (minority) shareholders	33
2.5. Information asymmetries in representative shareholder litigation	46
2.6. Conclusions	48
Notes	49
3. Report on arbitral proceedings involving collective rights of minority shareholders	67
3.1. Introduction	68
3.2. France	69
3.3. Germany	69
3.4. Israel	70
3.5. Italy	71
3.6. Portugal	72
3.7. Singapore	74
3.8. Spain	74
3.9. United Kingdom	76
3.10. United States	77
3.11. Considerations about Brazilian Law	82
3.12. Conclusions	91
Notes	92

4. Report on derivative litigation and collective arbitration in Brazil	109
4.1. Introduction	110
4.2. Derivative Lawsuits Under Brazilian Law	110
4.3. Derivative lawsuits against managers (directors and officers) (LSA article 159)	112
4.4. Issues for consideration/Recommendations	114
4.5. Derivative lawsuit against the controlling shareholder (LSA article 246)	116
4.6. Cost of the proceedings	117
4.7. Issues for discussions/Recommendations	119
4.8. Minimum ownership thresholds (LSA article 291)	122
4.9. Issues for consideration/Recommendations	122
4.10. Subsequent control over a derivative suit and settlements	123
4.11. Mechanisms to reduce the information asymmetry among shareholders, the company, the controlling shareholder and managers	124
4.12. Collective Arbitration Under Brazilian Law	125
4.13. Confidentiality	129
4.14. Issues for discussion/Recommendations	129
4.15. Conclusions	140

Notes	144
-------	-----

## TABLES

Table 1.1. Minimum number of asset managers to file a derivative lawsuit	11
Table 2.1. Overview of derivative litigation systems (Part 2)	29
Table 2.2. Litigation mechanisms involving the shareholder meeting (Part 3)	32
Table 2.3. Minimum percentages required for plaintiff groups in France	34
Table 2.4. Minimum percentages required for plaintiff groups in Brazil	42
Table 2.5. Derivative suits initiated by shareholders (Part 4)	45
Table 3.1. Main characteristics of the rules of arbitration of the arbitral institutions mentioned in the previous sections	81
Table 4.1. CVM rule on the minimum ownership percentages	122
Table 4.2. Proposals on derivative suits	141
Table 4.3. Proposals on collective arbitration	143



# 1. Summary of main findings and recommendations

## 1.1. Relevant goals for the private enforcement of shareholder rights

The annotations introducing Chapter 2 of the G20/OECD Principles state that “experience has shown that an important determinant of the degree to which shareholder rights are protected is whether effective methods exist to obtain redress for grievances at a reasonable cost and without excessive delay.” The annotations to the same principle also highlight that “there is some risk that a legal system which enables any investor to challenge corporate activity in the courts can become prone to excessive litigation.” Consequently, a balance must be struck by legislators and regulators between adequate incentives for investors to find redress for infringement of their ownership rights and avoiding frivolous litigation that may drain valuable resources from companies.

In its search for a reasonable balance between adequate incentives and legal mechanisms for investors to find redress while avoiding excessive litigation, the CVM/Ministry of Economy Task Force also gave consideration to the use of class action suits. However, in its workshop discussions with experts and stakeholders concerned with these issues, there was clearly more appetite in the Brazilian context to focus on reducing barriers to the use of derivative suits and reforms to facilitate the more effective use of arbitration as priorities for further consideration. Therefore, this review has focused on international experience with respect to these two issues, while drawing upon concepts and experience with respect to class action suits in some jurisdictions that may offer additional relevant insights for consideration of Brazilian reforms to its frameworks for derivative actions and arbitration.

## 1.2. Key points on derivative litigation

In line with the abovementioned goals, the chapter comparing the rules applied to derivative actions (i.e., lawsuits initiated by shareholders on behalf of the company against corporate fiduciaries – directors, officers and, in some countries, controlling shareholders) covers the following central issues.

Reviewed jurisdictions have established various procedures aimed at protecting against non-meritorious litigation. Some countries require the shareholder meeting to be involved in the decision to allow the initiation of a lawsuit on behalf of the company (only Brazil and Spain among the nine surveyed countries) while other jurisdictions make it optional (Germany and Italy). While the goal of such a rule is understandable, it might introduce considerable delays into the process. To reduce the same risk of frivolous litigation, some countries adopt screening mechanisms, such as minimum share ownership requirements to file a derivatives lawsuit (e.g., Brazil, Italy and Spain); or a pre-trial procedure to evaluate whether the claim is non-meritorious (e.g., Delaware in the US, Germany, Israel, Singapore and the UK).

A number of disincentives exist that may discourage or prevent the use of derivative lawsuits in surveyed jurisdictions. The financial risk of having to pay court fees and other litigation expenses in case of losing

the dispute is likely the most relevant disincentive for a minority shareholder to initiate a derivative action. This disincentive is exacerbated by the fact that the shareholder would only benefit from the remedy in proportion to his or her stake in the shares of the company. The obligation to reimburse the litigation costs to the winning party is the general rule in Brazil, France, Germany, Italy, Singapore, Spain and the UK. A possible solution to sufficiently reduce such risk would be to establish a pre-trial procedure (mentioned in the item above). Such a procedure would serve not only to evaluate whether the claim is non-meritorious, but also as a cut-off point after which the corporation (for whose benefit the derivative suit is brought) must bear litigation cost (this is the rule in Germany and Israel).

Due to the time and costs that a litigation process may incur, it may be in the interest of the company to have the derivative action settled in some circumstances. Such possibility may also be relevant to the shareholder considering the initiation of a lawsuit. Therefore, some countries have rules to clarify that the shareholder may settle the suit on behalf of the company and establish procedures to manage the conflicts of interests of the shareholders as a whole and the representative plaintiff (e.g., in Germany, Italy and Spain, the settlement must be reviewed by the shareholders meeting; and in Delaware, Israel, Singapore and the UK, the court must approve the settlement).

Another incentive for derivative actions is the possibility that attorney's fees may depend on the outcome of the lawsuit (e.g. the legal representative receiving a percentage of the award). This practice is feasible in the US and has proved to be one of the forces influencing the volume of lawsuits in the country. In Brazil, there are also few limitations on contingent and conditional fees and, in fact, instead of reimbursement of attorney's fees, the law provides for a contingent award to the winning plaintiff's attorney (20% in the case of derivative lawsuits against controlling shareholders and between 10% and 20% when directors and officers are the defendants).

One last issue impacting the feasibility of derivative actions is the asymmetry of information between, on one side, minority shareholders and, on the other side, managers or controlling shareholders, before the filing of the derivative lawsuits. In most systems, plaintiffs must have gathered some evidence before filing a lawsuit (at least to make a *prima facie* case or to be able to list which documents the management of the company must present) and, therefore, their chances of finding redress are low if the infringement of their ownership rights is not clear in public documents, such as financial and audit reports. Some instruments to reduce this information asymmetry are the discovery period in US law (during which plaintiffs with a thin basis of evidence may rely on the defendant's obligation to disclose pertinent information), and the judicial appointment of a special auditor or investigator upon the request of minority shareholders (as in France, Germany and Italy).

### 1.3. Recommendations on derivative litigation

The research and analysis of the derivative suits framework in Brazil has identified a number of weaknesses that the following proposed reforms aim to address. These include procedural barriers that minority shareholders must surpass before filing the derivative claim, such as annulling the exoneration of directors and officers from liability by the shareholders meeting. Likewise, the cost allocation between the winning and losing parties was identified as one of the main disincentives for effective private enforcement through derivative lawsuits. Finally, the current impossibility for the settlement of a derivative lawsuit is another disincentive for the use of derivative suits in the country<sup>1</sup>.

#### 1.3.1. *Extinction of the quitus*

According to the Brazilian Company Law (art. 134, paragraph 3), if the shareholders approve the financial statements and management's accounts without qualification in the annual shareholders meeting, the directors and officers are exonerated from liability for their conduct while in office during

that year (exonerating effect known as *quitus*). The exoneration covers even management conduct that was not explicitly referred to in the financial statements and in other documents presented to the shareholders meeting.

A derivative lawsuit, therefore, can only be initiated after the minority shareholders face the intricate problem of annulling the approval of the management's accounts, which is only possible within two years after the approval (art. 286). The hurdle is especially high in that case because the shareholder who files for the annulment must collect enough evidence to prove fraud, error, wrongful intent or simulation by the directors and officers.

In line with the existing rules in France and Germany, the Brazilian Company Law could be amended to **extinguish the exonerating effect of the approval of the managers' accounts or**, in line with the framework in Italy and Portugal, **establish that only an express resolution based on properly disclosed facts – which could be blocked by a qualified minority of shareholders** (20% of the stock in Italy and 10% in Portugal) – **would have exonerating effects.**

### **1.3.2. Establish a pre-trial procedure and change the allocation of costs**

The Brazilian Company Law presents three other obstacles besides the *quitus* for shareholders who want to file a lawsuit on behalf of the company against corporate fiduciaries:

1. a minimum share ownership requirement to file a derivative lawsuit;
2. the condition that the lawsuit must first be proposed at the shareholders meeting in the case that directors and officers are the potential defendants; and
3. the rule that the costs of the litigation must be fully borne by the minority shareholders that filed the lawsuit if they lose the dispute.

The minimum share ownership requirement is the amount shareholders must collectively own in order to be able to file a derivative lawsuit on behalf of the company. It is one of various forms to reduce the occurrence of non-meritorious derivative suits. There are a few exceptional circumstances in the Brazilian legislation when shareholders are not required to meet the ownership requirement, such as when the shareholders meeting approves the filing of a lawsuit but the officers fail to file within 3 months of the shareholder approval<sup>2</sup>.

In the case that directors and officers are the potential defendants, there is also the requirement that the lawsuit must first be proposed at the shareholders meeting (art. 159, para. 4). It can be proposed in any annual shareholders meeting or, in an extraordinary shareholders meeting, if it was previously included in the agenda or if it is closely related to an item in the agenda. The minimum ownership requirement for shareholders to call an extraordinary meeting is the same as the one to file a derivative lawsuit, and it would take up to 23 days for an extraordinary meeting to take place after the shareholders have called it.

In any case, the costs of the litigation must be fully borne by the minority shareholders that file the lawsuit if they lose the dispute, including the payment of the contingent award to the winning plaintiff's attorney. The financial risk of having to pay court fees and other litigation expenses in case of losing the dispute is, according to the comparative research on derivative lawsuits attached, likely the most relevant disincentive for a minority shareholder to initiate a derivative action. Specifically, in jurisdictions where plaintiffs are exposed to the full financial litigation risk, derivative suits by minority shareholders are uncommon.

Experience has demonstrated that those three obstacles together with the *quitus* have made the use of derivative lawsuits extremely rare in Brazil. As a result of research conducted by the OECD and discussions held during this project, CVM enacted in June 2020 a new rule that reduced the first two deterrents highlighted above.

The Brazilian Company Law establishes a 5% minimum share ownership requirement to file a derivative lawsuit (art. 159, para. 4 and 5, and art. 246) and to call an extraordinary shareholders meeting (art. 123), but CVM has the power to reduce the ownership requirement for listed companies (art. 291) and effectively did so through Rule CVM 627:

- for listed companies with outstanding capital stock<sup>3</sup> above BRL 10 billion (c. USD 2 billion), the requirement is now 1%;
- for companies with outstanding capital stock between BRL 5 billion (c. USD 1 billion) and BRL 10 billion, it is now 2%;
- between BRL 1 billion (USD 200 million) and BRL 5 billion, 3%;
- between BRL 100 million (USD 20 million) and BRL 1 billion, 4%;
- below BRL 100 million, 5%.

While it is an effective instrument to prevent frivolous derivative lawsuits, a minimum shareholder ownership requirement if set too high has the potential to impede lawsuits that are meritorious if minority shareholders cannot coordinate efforts to reach the minimum ownership required. This hurdle has become easier to overcome with the abovementioned CVM regulation. In order to evaluate the practical impact of the new CVM regulation, one could project some scenarios and analyse publicly available data on investment funds' equity holdings.

For the projection of scenarios, the following was considered:

- 1% of one of the biggest Brazilian listed companies (e.g., Itaú Unibanco, Vale or Petrobras) would represent c. USD 500 million (this would be the market value of the stock that minority shareholders would have to own to file a derivative lawsuit in those cases or to call an extraordinary shareholders meeting)<sup>4</sup>;
- 2% of a medium but still liquid<sup>5</sup> listed company (e.g. CPFL Energia) would represent c. USD 100 million;
- a successful active asset manager without any link to financial groups would typically manage between USD 1 billion and USD 2 billion in equities in Brazil (e.g., Dynamo and SPX). Likewise, in terms of composition of their portfolios, they would seldom have more than 5% invested in one single company and, in many cases, they would have more than 1%<sup>6</sup>.

Three realistic scenarios would be the following:

1. If some asset managers own c. USD 100 million (5% of a portfolio in a company times USD 2 billion of assets under management) in one major company's stock, *five asset managers* together would be able to reach the USD 500 million threshold to call an extraordinary shareholders meeting to propose the lawsuit and, if their proposal is not approved, file a derivative action;
2. If some asset managers own c. USD 30 million (3% of a portfolio in a company times USD 1 billion of assets under management) in one major company's stock, *seventeen asset managers* together would be able to reach the USD 500 million threshold;
3. If some asset managers own c. USD 10 million (1% of a portfolio in a company times USD 1 billion of assets under management) in one medium company's stock, *ten asset managers* together would be able to reach the USD 100 million threshold.

While the scenario analysis above is easy to understand and allows one to consider only active asset managers without any link to financial groups, it is based on some assumptions that might not be confirmed by more detailed data. In order to complement the analysis, it is therefore relevant to analyse the actual equity holdings of asset managers through investment funds incorporated in Brazil<sup>7</sup>. In the table below, it is possible to observe the minimum number of asset managers that would need to

coordinate efforts to call a shareholders meeting and to file a derivative lawsuit in each of the 50 biggest listed companies by market value according to the ownership requirements set by the new Rule CVM 627.

Table 1.1. Minimum number of asset managers to file a derivative lawsuit

Minimum number of asset managers to reach the threshold	Number of companies	Proportion in relation to the 50 most valuable listed companies
1	20	40%
2	12	24%
3	4	8%
Between 4 and 10	5	10%
Between 11 and 20	2	4%
Impossibility	7	14%

Notes: 1 The equity holdings of the investment funds incorporated in Brazil are as of 30 June 2020.

2 Equity holdings were aggregated by asset manager (“gestor” in Portuguese) in the case they managed more than one fund. In cases where an investment fund had more than one asset manager, one of the asset managers was randomly identified as the sole asset manager to avoid double counting.

3 When defining the ownership threshold for each company, market value was used as a proxy for outstanding stock capital.

4 In the last row of the table, “impossibility” means that, even if all asset managers with funds incorporated in Brazil could coordinate their efforts, they would not be able to reach the threshold to call a shareholders meeting or to file a derivative lawsuit.

Source: Data on investment funds’ holdings downloaded from

[http://www.cvm.gov.br/menu/acao\\_informacao/dadosabertos/dadosabertos.html](http://www.cvm.gov.br/menu/acao_informacao/dadosabertos/dadosabertos.html) on 5 October 2020. Analysis done by the OECD Secretariat.

Table 1.1 shows that, for 20 companies among the 50 biggest by market value, the asset manager with investment funds incorporated in Brazil with the largest shareholding in an individual company would be able to reach the threshold to call an extraordinary shareholders meeting and to file a derivative lawsuit. In a similar way, for 12 companies among the 50 biggest by market value, two of the asset managers with the largest shareholdings in an individual company would be able to reach the threshold to call a shareholders meeting and to file a derivative lawsuit. In the last line in the table above, it can be seen that, for seven companies among the 50 largest by market value, investment funds incorporated in Brazil hold an insufficient number of shares to collectively call an extraordinary shareholders meeting and to file a derivative lawsuit. In these cases of impossibility, asset managers would have to coordinate efforts with other institutional investors to call a shareholders meeting or to file a derivative lawsuit.

The main limitation in the analysis above is that it includes asset managers whose business models might not favour a more confrontational relationship with directors, officers and controlling shareholder even when filing a derivative lawsuit is clearly in the best interest of the final beneficiaries of the fund (for example, managers of passive funds). While it was not possible to filter out from the dataset passive funds and asset managers linked to financial groups, the analysis above was rerun to test its sensitivity to a situation where the asset manager with the largest share ownership in each company would not be willing to coordinate efforts to file a derivative lawsuit (the rationale is that passive funds and funds managed by conglomerates with large distribution channels typically have significant assets under management). The results, however, were not significantly different: instead of 41 companies with a minimum number of 10 or fewer asset managers to reach the threshold (as in Table 1.1), there would be 36 companies in the same group if the asset manager with the largest share ownership in each company were excluded from the dataset.

Based on the scenarios and data analysis above, it is possible to conclude that the typical number of investors that must coordinate efforts to file a derivative lawsuit – no more than 10 investors in most cases for the 50 most valuable companies – appears to have become reasonable after the enactment

of Rule CVM 627<sup>8</sup>. Of course, the investor who is leading the effort will probably have to contact a greater number of investors to guarantee the necessary number of shares; however, it should not be impossible if the apparent infringement to the ownership rights is clear and the financial incentives to file the derivative lawsuit are adequate.

The financial incentives to file the derivative action in Brazil, however, do not seem optimal and are clearly in dissonance with other more developed jurisdictions analysed in this comparative review of derivative lawsuits. A theoretical example might be useful to understand the rational decision-making process that minority shareholders would have to go through before filing a derivative lawsuit. As a reference, we can imagine that a major listed company with a market value of c. USD 50 billion is involved, and that there is evidence of an infringement of ownership rights that caused a loss to the company of c. USD 3 billion<sup>9</sup>. The possible payouts for the minority shareholders owning 1% of the major company's stock would be the following:

1. If the shareholders are successful, they will indirectly receive USD 30 million (1% of the USD 3 billion paid to the company) through the increase in value of the shares they own and, if the defendants are the controlling shareholders, directly USD 150 million as a premium (para. 2 of art. 246 of the Company Law establishes a 5% premium to the shareholders who sponsored the derivative lawsuit against a controlling shareholder); or
2. If the shareholders lose the dispute, they will have to pay for all the costs of the litigation, including court fees, their own legal representatives and the payment of a contingent award to the winning plaintiff's attorney (20% in the case of lawsuits against controlling shareholders and between 10% and 20% when directors and officers are the defendants). In this example, just considering the contingent award, minority shareholders would then have to pay between USD 300 million and USD 600 million (most likely the latter since a shareholder would hardly initiate a lawsuit for a USD 3 billion loss against directors and officers).

Still on the example above, someone might argue that, if evidence on the wrongdoing was effectively transparent, minority shareholders would still be willing to file the lawsuit. In this example, nevertheless, the expected chance of success would have to be 76.9% for risk-neutral shareholders to be indifferent between filing and not filing a derivative lawsuit only considering the possibility of having to pay the contingent award of USD 600 million<sup>10</sup>. In reality, however, most investors are risk-averse (i.e., they require to be compensated for the risk they assume) and shareholders would have to cover other litigation costs<sup>11</sup>, therefore virtually eliminating any chance that a rational minority shareholder would be willing to sponsor the lawsuit in the example presented<sup>12</sup>.

Alternatively, if the litigation costs were covered by the company after a pre-trial procedure (as previously mentioned, this is the case in Germany and Israel), the payouts for the minority shareholders owning 1% of the major company's stock would be the following in the same context of the prior example:

1. If the shareholders are successful, they will indirectly receive USD 30 million through the increase in value of the shares they own directly and, if the defendants are the controlling shareholders, USD 150 million as a premium; or
2. If the shareholders lose the dispute, they will indirectly lose somewhat more than USD 6 million (1% of the USD 600 million disbursed by the company as a contingent award to the winning plaintiff's attorney plus other litigation costs).

In this alternative example, the expected chance of success would have to be 3.2% for risk-neutral shareholders to be indifferent between filing and not filing a derivative lawsuit<sup>13</sup>. Nevertheless, it should be noted that, in practice, the percentage will be higher because investors are as a rule risk averse, and face other costs if they lose the dispute (e.g., paying their own legal representatives if they are unsuccessful in the pre-trial and the opportunity cost of their time). This alternative threshold would likely

allow minority shareholders with sufficient evidence to support a case to file the derivative lawsuit on behalf of the company.

In line with the existing rules in Germany and Israel, the Brazilian Company Law could be amended to **establish a pre-trial procedure, which would serve not only to evaluate whether the claim is non-meritorious but also as a cut-off point after which the corporation must bear litigation costs even if the lawsuit is ultimately unsuccessful**. In relation to the criteria for the judicial screening, Brazil could either follow the German model (an analysis of whether the suit is likely in the best interests of the corporation and if plaintiffs have a *prima facie* case) or the Israeli one (in addition to the criteria set in the German model, an assessment of the plaintiffs' motive). The Delaware pre-trial procedure model may be less fitting for Brazil (i.e., requiring an evaluation of whether management would not be best positioned to file a lawsuit on behalf of the company), because the intricate relationships between directors and controlling shareholders in a country like Brazil usually involving companies with defined control might rarely leave directors and officers free of any conflict of interests.

The requirements of minimum share ownership and that the action must first be proposed at the shareholders meeting could also be abolished, because the court would be responsible for screening non-meritorious lawsuits. This alternative to abolish both mentioned requirements would be in line with most jurisdictions covered in this review. Nevertheless, since the enactment of Rule CVM 627, both requirements have become much less burdensome for minority shareholders and, therefore, their abolishment might be a less immediate priority. Sequencing the decision on the extinction of the two requirements would also permit policymakers to evaluate whether the pre-trial procedure functions well in practice before eliminating these two additional barriers for non-meritorious derivative lawsuits.

### **1.3.3. Regulate derivative lawsuits settlements**

Despite the lack of specific provisions in the Brazilian Company Law, legal scholarship argues that the shareholders cannot settle the claim in a derivative suit on behalf of the company. The argument is that, while the plaintiffs in a derivative lawsuit are acting on behalf of the company, they do not have authority to waive the company's rights. In other words, the shareholders could settle, but the settlement would not bind the company and, therefore, defendants would most likely not be interested in agreeing on a settlement.

Due to the time and payments that a litigation process might demand, however, it might be in the interest of both the company and the plaintiffs to settle the derivatives action in some circumstances.

Nevertheless, settlements of derivative lawsuits agreed between only some shareholders and the defendants might not be in the interest of the company and its shareholders. For instance, there might be the incentive for the parties to collude<sup>14</sup> to end a promising derivative suit in exchange for an unusually high payoff for the shareholders' attorney or a non-financial obligation inserted in the settlement that would especially favour the shareholders sponsoring the lawsuit.

Because of the abovementioned risk, some countries have established procedures to manage the conflicts of interest between the shareholders as a whole and the representative plaintiff in the case of settlements of derivative lawsuits. Those procedures are of two different types: (i) in Germany, Italy and Spain, the settlement must be approved by the shareholders meeting with a right for minority shareholders to block the settlement (for listed companies, shareholders owning 10% in Germany, 5% in Italy and 3% in Spain); (ii) in Delaware, Israel, Singapore and the UK, the court must approve the settlement. In the case of Israel, in addition to the court deciding whether the settlement is adequate, the Israel Securities Authority also reviews whether the settlement is in the interest of all shareholders. Likewise, a rule that was suggested in the 2020 Workshop – but which does not apparently exist in any jurisdiction – would be to impede counsel from receiving fees in an early settlement in order to

disincentivise derivative lawsuits financially sponsored by attorneys with the sole purpose of rapidly settling the dispute for their sole private benefit.

In the Brazilian context, it could be problematic to rely on the review by the courts or the capital markets regulator, because, despite all their merits, their resources are scarce and should be allocated judiciously. The alternative solution of requiring the approval by the shareholders meeting – with blocking rights by a minority of shareholders – may be the best solution. In relation to the amount of shares, it is worth noting that the amount of shares to block a settlement is the same as the number of shares necessary to bring derivative suits in Spain, thus ensuring that plaintiffs can prevent the corporation from taking the suit out of their hands. In Italy, the amounts are the same in the case of private companies, but the threshold to block a settlement is slightly higher than the one to file a derivative lawsuit for public companies (respectively, 5% and 2.5%). In Germany, the amount of shares necessary to block a settlement is higher than the amount required to file a derivative lawsuit as well, but a settlement is permissible only three years after the claim arose.

It would, therefore, be expedient to **clarify, in the Brazilian Company Law, that the shareholder might settle the derivative suit on behalf of the company after the approval by the shareholders meeting with blocking rights to shareholders owning the same amount of shares necessary to file a derivative lawsuit.**

#### 1.4. Key points on arbitration

Brazil and Spain are the only jurisdictions among the 10 covered in this review that have opted for arbitration as a means of resolving corporate and securities disputes involving publicly listed companies. The Brazilian Company Law not only recognizes that the articles of incorporation may include mandatory arbitration clauses, but the adoption of such a clause is also a condition for companies to be listed in the B3's listing segment with the highest standards of corporate governance ("Novo Mercado"). This growing reliance on arbitration for resolution of corporate disputes – as mentioned in the OECD 2013 publication *Supervision and Enforcement in Corporate Governance* (pp. 59 and 60) – stems from the (i) slow pace of the Brazilian judicial system in conducting proceedings, and (ii) some judges' lack of good knowledge of corporate law issues.

Possibly because of the properties of inertia, corporate and securities arbitrations in Brazil are protected by confidentiality restrictions in the same way that commercial arbitration traditionally has been. Confidentiality of arbitration proceedings involving shareholders' ownership rights, however, create a number of challenges for the efficient working of the capital markets, and a reform is recommended below to increase disclosure of arbitral proceedings involving listed companies. Disclosure of arbitration proceedings involving public companies has become even more relevant in Brazil more recently due to the initiation of several collective arbitrations involving major listed companies, which became public only through relatively brief disclosures of material facts and press reports.

Another consequence of the broad adoption of arbitration by listed companies in Brazil is that derivative claims can be solved in an arbitration framework that was designed mainly for commercial disputes with two parties. This means, for example, that the choice of arbitrators and the model of cost allocation can be freely decided on a case by case basis, whereas derivative claims involve a great number of potentially affected shareholders that may not intervene directly in the proceedings. Another set of reforms is therefore proposed in this chapter to deal with this challenge.

Although Brazil clearly makes much wider use of arbitration for the resolution of shareholder disputes than the other nine jurisdictions reviewed for this publication, the experience and legal frameworks of these jurisdictions can nevertheless provide a basis for a number of useful insights which could help Brazil to improve the functioning of its framework.



The chapter comparing the rules – not only legal but also internal rules of arbitral institutions – applicable to collective arbitration (i.e., arbitrations that allow for a group of claimants to advance their claims collectively in one action against a single respondent or a group of respondents) covers the following central issues.

Publicity of the main phases of an arbitration proceeding is a necessary – though not sufficient – condition for the existence of collective arbitrations involving the enforcement of shareholders' rights. Especially in the case of publicly listed companies, shareholders may find it difficult to coordinate efforts to hire a law firm and file the request for an arbitration proceeding and, therefore, it is necessary that the shareholders are promptly informed in regards to the filing of the request in order for the greatest number to intervene. This is the rule, for example, for proceedings initiated in one arbitration institution in Germany and two others in the US covered by chapter 3 (in Germany, the rules mentioned here are for non-listed companies, since disputes over collective rights of minority shareholders of publicly held companies are not arbitrable in mentioned country).

Arbitration involving collective interests of shareholders can follow either an opt-in system (where shareholders need to adhere as parties to the proceeding) or an opt-out one (where every shareholder is considered represented by the plaintiff if the shareholders do not pronounce otherwise within a deadline at the beginning of the proceeding). The opt-out system is considered advantageous for the goal of fostering collective arbitrations because – for psychological and practical reasons – it results in a greater number of shareholders being represented in the dispute and, therefore, bound by the arbitration award (it has arguably been one of the main reasons why class actions are so common in the US). Of course, an opt-out system would only be fair if the initiation of an arbitration proceeding is efficiently publicised to all shareholders and if they have sufficient time to analyse the claim and decide whether it would be in their interest to stay as a party.

In any case, none of the 10 jurisdictions covered in chapter 3 have an opt-out collective arbitration system for corporate disputes, which one could refer to as “class arbitration”. What does currently exist are some multiparty arbitrations initiated by shareholders who brought together a claim to an arbitral institution, but who do not represent any other shareholder that did not formally accept to be a party.

It was identified that, in jurisdictions where there is a specific framework for shareholders' arbitrations, it is usually possible to consolidate proceedings with similar claims (e.g., in Germany and Spain), which has evident advantages from an efficiency point-of-view. However, it is important to observe that, if an opt-out arbitration system would be adopted, the appeal of consolidating proceedings would likely be smaller, due to the potential of the opt-out system to reunite a great number of shareholders as represented parties.

The last two chapters of this document also cover rules related to other issues such as the following:

1. If the intervention of a third party is admissible after the appointment of the arbitrators, then those third parties should have to accept the composition of the arbitral tribunal as prescribed in the rules of two Spanish arbitral institutions covered in chapter 3;
2. Both in class actions and collective arbitrations, one of the most important steps of the proceeding is the class certification, whereas the court or the arbitral institution define the class, its representative and counsel, based on set guidelines that may include, for example, number of shares represented, previous experience regarding collective disputes and the relevant legislation, potential conflicts of interest and financial capacity;
3. Private arbitration has higher direct costs than court litigation and, therefore, one common concern is whether small minority shareholders would be able to afford filing an arbitration request if they will have to cover a considerable part of the costs of the proceeding.

## 1.5. Recommendations on corporate arbitration

The subsequent chapters of this review do not focus on the discussion of whether the adoption of mandatory arbitration clauses should be possible for public companies, although arbitration involving publicly listed companies is either not permitted or not common in jurisdictions reviewed except for Brazil. Rather, as this project is focused on insights to be gained for application to the Brazilian framework, chapters 3 and 4 present alternatives to improve arbitration as an instrument to solve disputes between shareholders of public companies and their managers or controlling shareholders, focusing particularly on its use for collective arbitration.

The last two chapters of this review contain proposals to establish – or at least make possible – an opt-out system in corporate arbitrations, including the clarification that shareholders should have the right to opt-out during the first phase of the proceeding and if a settlement is proposed to the class of shareholders. While both chapters provide good arguments in favour of such a reform, there remain some arguments to suggest that the Brazilian government should move cautiously in this regard:

1. Currently, arbitrations involving shareholders' ownership rights are completely confidential in Brazil. Whereas they should become more transparent to all shareholders as argued below, it is still uncertain how a reform on the disclosure of corporate arbitrations would play out in practice. If a reform on this front were not as successful as planned, the adoption of a class arbitration would risk allowing considerable power to some plaintiffs representing the class of shareholders but without the necessary public scrutiny.
2. Brazil does not have any instrument equivalent to a class action that has proven to function in practice. Moreover, there are not many examples to draw upon from other Civil Law jurisdictions of class action frameworks that have been thriving. Thus, although possible if the legislation were altered, it would be at a minimum startling within the Brazilian legal tradition to introduce a rule binding shareholders that were not formally parties in a proceeding.
3. Such a rule or a practice has not been implemented – to the best of our knowledge – by any OECD members and, therefore, there is a lack of real world experience to assess its effectiveness in practice.

The reviews undertaken for this publication and the discussions during the 2020 Workshop, in any circumstance, have provided relevant insights for possible reforms of the corporate arbitration framework in Brazil. The following recommendations have been identified for expeditious adoption by the Brazilian government.

### **1.5.1. Disclosure of arbitrations involving shareholders' ownership rights**

Arbitral proceedings are confidential in the most used arbitration institutions in Brazil. However there is no legal provision requiring such confidentiality. While companies and their managers may seek to resist enhanced scrutiny of shareholder disputes that transparency may bring, keeping confidentiality as the rule creates three main challenges: (i) shareholders who might be affected by decisions of the arbitrators do not have the opportunity to intervene in the proceeding; (ii) arbitral decisions lose their reputational effects, which might be important to deter mismanagement and abuse; (iii) market participants lose an important source to understand what their duties as managers and controlling shareholders effectively mean in concrete cases. While abovementioned challenges are significant, it was not possible to identify a major benefit for the development of the capital markets due to the confidentiality.

The disclosure of the initiation of an arbitral proceeding involving shareholders' ownership rights would also have the advantage of allowing larger multiparty arbitration proceedings than are currently possible. In the case of publicly listed companies, shareholders may find it difficult to coordinate efforts to hire a

law firm and file the request for an arbitration proceeding. However, if all shareholders are promptly informed with regard to the filing of a request for arbitration, a broader group of shareholders might intervene, generating economies of scale and risk-sharing opportunities at a level similar to what would exist in a collective arbitration with an opt-out rule.

In the case of a proposed settlement that might affect all shareholders, transparency is also essential to reduce the possibility of collusion among the plaintiffs, defendants and their attorneys that might not be in the best interest of the company. If all shareholders are informed of the content of a settlement before it is closed, it will be possible for them to take adequate actions and, therefore, avoid possible damages.

In line with arbitration institutions in Germany and in the US, it therefore would be desirable to **require Brazilian public companies and their controlling shareholders to publicise sufficient information on the main phases of the arbitral and judicial proceedings involving shareholders' rights from the filing until the final award.**

CVM already has the power to enact a regulation requiring the abovementioned disclosure and is well-positioned to draft an effective one; however it is worth highlighting some aspects related to scope and form of the proposed regulation that should be taken into consideration.

Disclosure requirements should be broadly encompassing. Currently some arbitration proceedings are disclosed as a consequence of the general requirement that the market should be promptly informed on facts that may materially affect the business of the company. The disclosure, however, should address not only material impacts. As previously mentioned, disclosure of the proceedings should have not only the objective to improve the price discovery feature of the capital markets, but also the goals of allowing other shareholders to join the dispute, ensuring the reputational effects of arbitral decisions and opening a relevant source of precedents to market participants. Having those objectives in mind, the disclosure should also include disputes brought to the Judiciary, because, while judicial proceedings are public as a rule, the dissemination of the start of a judicial proceeding will be broader and will expedite use of the ordinary channels through which the public company communicates with the market.

In relation to the types of disputes, at a minimum the following proceedings should be disclosed: (i) when the claim is a derivative or a collective one; and (ii) if the decision may affect other shareholders' rights (e.g., the annulment of the shareholders meetings' resolutions). In both cases, shareholders should have sufficient information on the dispute because they might want to intervene in the proceedings. Nevertheless, as previously observed, allowing the opportunity to intervene is not the sole rationale behind the disclosure and, therefore, all disputes involving shareholders' rights may have to be made public. For example, while a dispute among parties of a shareholders agreement may not directly affect the rights of other shareholders, it might still be relevant for the future business perspectives of the company, have reputational effects for the parties involved and constitute an important precedent for shareholders in other companies.

Corporate judicial or arbitral case files, however, may indeed have some documents that would deserve (at least partially) confidential treatment in the best interest of the company. Courts are used and have clear guidelines to that nature of judgement and, therefore, if a piece of information is deemed public by the judiciary, there is no reason for the company to conceal it. Brazilian arbitral institutions, however, have been operating under full confidentiality and a move to publicity as the rule would have to rely on one or a combination of the following three stakeholders: the arbitral institutions; the companies; the capital markets regulator. Arbitral institutions, however, are not CVM regulated entities and, therefore, the regulator could not impose any duty to them.

There are chiefly three forms of sharing the burden of the analysis between the public company and CVM in relation to what should be disclosed to the market. At one extreme, the company would send all case files to CVM and its staff would prepare a report to be disclosed with relevant information. This solution does not seem feasible, however, because of those proceedings' complexity and the scarce

resources available to the regulator. At another extreme, the company would decide what to publicise and, on a case by case basis, the regulator might request further disclosure. While this approach may be adequate after a body of case law has been established, it would allow directors, officers and controlling shareholders an ample latitude to conceal relevant information in the short-term. A middle-of-the-road solution may be the most effective: CVM could create a form to be published on its website listing which pieces of information the company would have to disclose in different steps of the dispute (at least shortly after the filing, when the terms of reference are signed, when a settlement is proposed and at the final award). CVM has created a similar form for related parties' transactions – for which similar conflicts of interests exist – and, while good quality disclosure will still depend on effective enforcement and market participants' oversight, the form on arbitration proceedings will provide some guidance for companies from the moment the regulation is enacted.

A last issue that CVM should consider when regulating the disclosure of arbitration and judicial proceedings involving shareholders' rights is that the company may not be a party in the dispute. For instance, this would be the case in a derivative or a collective claim against the controlling shareholder or former managers. For those cases, shareholders or former directors and officers must be obliged to provide the relevant information for the company to fulfil its disclosure duty.

### ***1.5.2. Align rules applicable to arbitrated derivative actions***

Derivative actions can be solved through arbitration in Brazil only if, like any other lawsuit involving shareholders rights, company's articles allow it. It does not mean, however, that the same procedural rules related to cost allocation, contingent awards and premium to the successful plaintiff equally apply to an arbitrated derivative action. In fact, companies' articles, arbitral institutions' rules or arbitral agreements are free to stipulate how the costs will be shared between the parties. Moreover, contingent awards to the winning party's legal representatives (between 10 and 20% as previously detailed in this chapter) and the 5% premium for the plaintiff in successful derivative suits against controlling shareholders do not exist as a rule if the derivative claim is arbitrated.

In Brazil, the general practice is for arbitral agreements and the arbitral institutions' rules to set forth that the losing party must reimburse the winning party for all costs except for the attorney fees (most importantly, the compensation of arbitrators and experts called to support the proceedings). Despite the best efforts made during this review, it was not possible to assess the average cost of an arbitration proceeding. However more than one source suggested that costs of arbitration may be high for minority shareholders.

In relation to the formation of the arbitral tribunal in different jurisdictions, the arbitrators are typically appointed by the parties or by the arbitration centre. In Brazil, the parties usually appoint the members of the arbitral tribunal, following the rule that each party appoints one arbitrator and the two chosen arbitrators select the presiding arbitrator. While the selection process by the parties might work well for commercial disputes, it is debatable whether it would be the best model for disputes that may affect other shareholders who are not parties in the proceeding and, therefore, could not influence the appointment of the arbitrators.

It would be prudent, therefore, to **establish in the Company Law that the same rules related to cost allocation, contingent awards and premium to the successful plaintiff that apply to derivative claims brought to the Courts should be binding if the claim is arbitrated**. Specifically, it should be clear that, in line with our previous recommendation, companies would have to cover arbitration costs where shareholders are requesting redress from managers or controlling shareholders on behalf of the company after a pre-trial procedure in which the arbitral tribunal would evaluate whether the claim is non-meritorious. This seems to be a balanced way to avoid that the high cost of arbitration or allocation rules that disfavour minority shareholders<sup>15</sup> would hinder achievement of effective redress for the violation of their rights.

Whereas there is not enough evidence – based on the attached chapters – to support the enactment of a legal rule requiring the appointment of the arbitral tribunal by the arbitral institution instead of the parties, three aspects should be taken into account.

First, as previously recommended, any settlement of a derivative action should be approved by the shareholders meeting with blocking rights to minority shareholders in order to avoid the risk of collusion among plaintiffs, defendants and their attorneys. The alternative rule of requiring the arbitral tribunal to approve the settlement presents some risks, because arbitrators chosen by the parties might face incentives not to treat equally the interests of shareholders who are not formal parties.

Second, more transparency on arbitration proceedings will be relevant to enhance the quality and impartiality of the decisions taken by the arbitrators, provided that their names are also disclosed (just like the names of the judges are disclosed in any judicial proceeding). This would not only increase the reputational costs to arbitrators for a biased decision but also, following the procedure set out by Law 9,307 of 1996, allow for the timely replacement of an arbitrator with any conflict of interests. Therefore, it would be advisable for **CVM to include in its disclosure regime the requirement for the company to publicise who the members of the arbitral tribunal are.**

Third, arbitral institutions – especially B3’s arbitration chamber<sup>16</sup> – should evaluate whether its internal rules should not require (i) the appointment of arbitrators by its secretariat – following clear and previously set criteria – in multi-parties corporate arbitrations and (ii) the consolidation of arbitral proceedings with similar claims (the consolidation is possible, for example, in the German and Spanish arbitral institutions covered in chapter 3s). The first requirement, besides the enhanced impartiality in relation to affected shareholders who are not parties, would make the appointment of the arbitral tribunal operationally easier in the case where there is a great number of formal parties. The latter requirement would not only improve the value for money of the arbitration proceedings, but also reduce the chance of conflicting decisions.

## 1.6. Other factors to consider

However essential an adequate regulatory framework for private enforcement of shareholders’ rights is, it should be noted that an effective protection to their ownership rights depends on other factors. For instance, the following three were highlighted in the 2020 Workshop:

- If directors’ and officers’ liability insurance policies (“D&O”) cover settlements and all personal losses those individuals might accrue if they are sued as a result of serving in corporations, they might not face optimal incentives to fully consider shareholders’ rights. However, consideration of exposing directors and officers to litigation risks must also take account of the potential that such exposure could deter qualified but extremely risk-averse individuals from serving in such positions.
- Judiciary or arbitral decisions that are unsound or untimely will not serve to protect the legitimate interests of minority shareholders. This might be the case, for example, if courts are clogged or arbitral institutions have lists of arbitrators that limit the selection of the best ones available to resolve the dispute.
- Institutional investors – who are the typical minority shareholders with capacity to proceed with a corporate dispute – might face disincentives to sue that are not strictly related to the private enforcement framework. For example, an asset manager might fear that the financial group it belongs to may lose fees in its investment banking activities if suing the controlling shareholder of a major corporation. While such a decision to remain inactive would likely be considered an infringement to the asset manager’s fiduciary duties, it would be extremely unlikely that the

regulator would be able to identify the possible irregularity and build a case against the asset manager.

The issues above are beyond the scope of the current project with CVM and the Ministry of the Economy, but could be considered in future projects or in meetings convened by the OECD.

## Notes

<sup>1</sup> While slow court processes and in some cases judges' lack of specialised expertise have previously been identified as a barrier to effective private enforcement actions, such issues have not yet appeared to be the most relevant barriers to derivative lawsuits. However, if legal reforms lead to more frequent derivative suits, the responsiveness of the judiciary could become an issue in the future. Taking this risk into account, this initial chapter presents two related recommendations. First, the possibility to settle could be a remedy to lengthy court processes, and this is one of the reasons why this chapter recommends a settlement to be possible and adequately regulated. Second, it should be noted that derivative lawsuits are arbitrable in Brazil, and one of the main concerns detailed further below is whether procedural rules designed for derivative lawsuits should be compulsory when they are solved through arbitration. The view expressed in this initial chapter is that some of the same general rules should apply to arbitrated cases and, if this recommendation is implemented, arbitration could be an acceptable alternative to crowded and unspecialised courts.

<sup>2</sup> Another exception is when the defendant is the controlling shareholder. In this case, shareholders who do not reach the ownership threshold can file a derivative lawsuit if they provide security for court costs and attorney fees that will become due if the suit is held groundless (art. 246, para. 1, item "b", of the Company Law).

<sup>3</sup> Outstanding capital stock is the value of the stock mentioned in the company's bylaws or articles, which differs from its market value. This is the only criteria that art. 291 of the Company Law allows CVM to use when reducing the ownership thresholds established in other provisions of the same statute.

<sup>4</sup> Information on market capitalisation was extracted from <https://finance.yahoo.com/> and information on registered share capital was obtained from companies' bylaws in <http://www.cvm.gov.br/menu/regulados/companhias/consultas/consulta-a-informacoes-de-companhias.html> on 18 August, 2020.

<sup>5</sup> Liquidity is evidently a relative concept but, here, it simply means that the share of the company is part of the main index and, therefore, likely to be followed by many fund managers.

<sup>6</sup> Information on assets under management of fund managers was obtained from [https://www.anbima.com.br/pt\\_br/informar/ranking/fundos-de-investimento/gestores.htm](https://www.anbima.com.br/pt_br/informar/ranking/fundos-de-investimento/gestores.htm) and on their portfolios from <http://www.cvm.gov.br/menu/regulados/fundos/sobre.html> on 18 August, 2020. Passive asset managers or active fund managers linked to financial groups – which often have more assets under management – were excluded from the projection of scenarios because of the specific disincentives they might face to file a derivative action against management or controlling shareholders.

<sup>7</sup> Data on the holdings of other equity investors, such as pension funds or investment funds incorporated abroad, are not publicly available for non-controlling shareholders with stakes below 5% in a listed company.

<sup>8</sup> An important presumption in this analysis is that statutory language permitting shareholders to bring derivative lawsuits (articles 154 and 246 of the Company Law) indicate that prior ownership (e.g., ownership at the time of the alleged wrongdoing) is not required. If this presumption is not correct, the minimum ownership requirement would be harder to reach because minority shareholders who have bought their shares after the alleged wrongdoing might not be able to support the filing of the lawsuit. Likewise, it should be noted that a prior ownership requirement would likely reduce the liquidity in a market that already suffers from low depth, because shareholders would have the incentive not to trade their shares if they believe a wrongdoing has taken place.

<sup>9</sup> This was actually the value of Petrobras' settlement in a well-known US class action lawsuit.

<sup>10</sup>  $x=76.9\%$  in  $x*(150+30)=(1-x)*600$ . In any case, it should be noted that  $x$  is the same regardless of the amount of the alleged loss if the equity ownership of 1%, the premium of 5% and the 20% of contingent award to the winning plaintiff's attorney remain constant (the last two variables are necessarily constant because they are fixed by the legislation). For example, for an alleged loss of USD 100 million,  $x$  would still be equal to 76.9% in  $x*(5+1)=(1-x)*20$ .

<sup>11</sup> Besides other litigation costs, it should also be considered that shareholders have the opportunity cost of the time they invest in coordinating efforts to file and advance the lawsuit.

<sup>12</sup> Following the same simplifying assumptions and calculation as in the example for a lawsuit against the controlling shareholders, the expected chance of success would have to be between 90.9% and 95.2% for risk-neutral shareholders to be indifferent between filing and not filing a derivative lawsuit against directors and officers. Those two extremes reflect, in the former percentage, a 10% of contingency award and, in the later case, 20% contingency award. The percentages are above 90% in the case of derivative lawsuits against directors and officers because there is no premium in the case of success, as there is when the defendant is the controlling shareholder.

<sup>13</sup> In the case of derivative lawsuits against directors and officers (where there is no premium for plaintiffs in the case of success), if the company were to cover the litigation costs after a pre-trial procedure, the expected chance of success would have to be between 9.1% and 16.7% for risk-neutral shareholders to be indifferent between filing and not filing a derivative lawsuit (respectively, considering the extremes of 10% and 20% for the expected contingency award).

<sup>14</sup> While collusion might beget civil and criminal liabilities, it may be extremely difficult to detect and prove it in practice. Likewise, some settlements against the interest of the company might exist solely because of the incentives for the involved parties without necessarily the intent to collude that would prompt the liability.

<sup>15</sup> Once again, it is important to remember that companies' bylaws and arbitral institutions' internal regulations might establish rules on cost allocation and contingency awards, without the participation of minority shareholders.

<sup>16</sup> B3's arbitration chamber ("Camara do Mercado" or "CAM") is one of the most relevant for corporate disputes in Brazil due to B3's listing requirements, which require all companies that are listed in Novo Mercado to include in their bylaws that corporate disputes should be solved through arbitrations conducted according to CAM's internal rules.





## 2. Report on derivative litigation

---

This chapter compares frameworks for derivative litigation in Brazil, France, Germany, Israel, Italy, Singapore, Spain, the United States and the United Kingdom. It was authored by Professor Martin Gelter.<sup>12</sup>

---

## 2.1. Overview

This chapter was drafted<sup>3</sup> for the OECD for consideration at its 2-3 December 2020 workshop organised in collaboration with the Brazilian Ministry of Economy and Brazil Securities Commission in order to support the Brazilian government's consideration of reform proposals for the law governing derivative litigation in Brazil. This chapter is intended to be considered in parallel with separate chapters to compare selected jurisdictions' frameworks for the use of collective arbitration by shareholders; and a chapter focusing on the legal framework specifically in Brazil and potential reform proposals related to derivative litigation and collective arbitration that take into account Brazil's existing legal framework and institutions. In that context, this chapter covers the corporate (company) law of four common law jurisdictions (the United States<sup>4</sup>, the United Kingdom<sup>5</sup>, Singapore<sup>6</sup> and Israel<sup>7</sup>) and five civil law jurisdictions (Brazil<sup>8</sup>, France<sup>9</sup>, Germany<sup>10</sup>, Italy<sup>11</sup> and Spain<sup>12</sup>). Among these countries, the US is known to make use of derivative suits most extensively. In all jurisdictions, this chapter refers to the law in force as of January 1, 2020.

Reform of shareholder litigation is nearly always controversial in any country. On the one hand, litigation is often considered an important right in the menu of options available to shareholders. Like anyone operating in an ineffective legal system, directors and officers not facing sanctions for violating their duties of care or loyalty may have insufficient incentives to comply with these (except e.g. reputational incentives affecting capital markets or managerial labour markets). When the corporation is harmed by such actions, shareholders typically only suffer a reflective loss because of the loss of the value of their interest. The proper plaintiff to enforce claims of the corporation is the latter itself, but often the alleged wrongdoers (including directors, officers, and controlling shareholders) are still in control of it.<sup>13</sup> Consequently, it appears to be necessary to create a mechanism for (minority) shareholders to initiate such litigation. At first glance, shareholders' incentive to sue looks weak. Plaintiffs only benefit from such a suit in proportion to their shares in the company, while the remaining benefits accrue to others. Nevertheless, they typically have to invest time and bear the cost.

On the other hand, facilitating litigation also engenders the possibility of abuse. A small likelihood of success, combined with negative publicity resulting from litigation, may mean that the corporation and its executives could spend time and money in a better way.<sup>14</sup> Directors and officers are usually in the best position to gauge advantages and disadvantages, which makes the decision to give minority shareholders the power to initiate and pursue litigation a difficult one. Moreover, shareholder litigation can sometimes appear to be abusive, especially when specialized law firms are among the main beneficiaries.<sup>15</sup> Lawyers may hope to receive a lucrative contingency fee because of a settlement.<sup>16</sup> The interests of lawyers rather than shareholders may therefore drive decisions taken during the procedure, a phenomenon called litigation agency cost.<sup>17</sup> Nevertheless, keeping this in mind it is entirely possible that this is an acceptable cost in order to create sufficient enforcement of directors' duties. Without anyone facing strong incentives to litigate, the deterrent effect of enforcement may be too weak (unless market mechanisms take over this role).<sup>18</sup> Without well-enforced duties, investors may lose confidence in firms and capital markets, which results in higher costs of capital for firms. They may thus decide to eschew markets entirely.

An effective litigation mechanism therefore needs to walk a tight line between over- and under-litigation. An ideal system will permit meritorious suits to go forward and shut down abusive ones at an early stage.<sup>19</sup> Thus, this chapter seeks to provide a comparison of several jurisdictions with mature legal frameworks to understand how different jurisdictions consider these trade-offs, and how different approaches may influence the efficiency and functioning of such measures.

The chapter looks at derivative suits and their close equivalent primarily in publicly traded corporations. Where a jurisdiction provides multiple corporate legal forms, we look at the type of corporation capable of and most commonly used to go public, i.e. the corporation (US), the public company (**Israel**<sup>20</sup>, **Singapore**<sup>21</sup>, **UK**<sup>22</sup>), the *Aktiengesellschaft* (**Germany**), the *société anonyme* (**France**), the *sociedad anónima* (**Spain**), the *sociedade anônima* (**Brazil**) and the *società per azioni* (**Italy**). The chapter only covers suits by shareholders (and not those e.g. by creditors).<sup>23</sup> **Brazil, Germany, Italy and Spain** also

permit the initiation of litigation against directors in the shareholder meeting. This form of litigation should probably not be described as derivative litigation but is still covered in this chapter (Section 2.3).

In the **United States**, approximately 50-60% of publicly traded corporations are incorporated in Delaware, which is why this chapter discusses primarily **Delaware** law<sup>24</sup>. Delaware law distinguishes between derivative and direct suits. Derivative suits provide redress for harm to the corporation, whereas direct suits concern harm directly inflicted on shareholders.<sup>25</sup> Most of the guiding principles of derivative litigation were developed in the case law over the course of the 20<sup>th</sup> century, although legislation, including the *Delaware General Corporation Law* (DGCL) and the applicable Rules of Civil Procedure<sup>26</sup> also play a significant role. The Delaware Court of Chancery, one of Delaware's courts of first instance, has (among other issues) jurisdiction over corporate law matters and is known as for the judge's specialized expertise in the field.<sup>27</sup> Given that suits can (depending on jurisdictional rules) also be brought in the federal courts or other state courts, the Federal Rules of Civil Procedure (and other states' rules) also play a role. Procedural rules tend to be very similar. On occasion, we will refer to the laws of other states and to the *Revised Model Business Corporation Act* (RMBCA).

The rest of this chapter is structured as follows. Part 2.2 surveys the overall structure of the system of derivative suits (and their close equivalents) in the nine countries. In particular, it surveys for what kind of claims such suits can be used, and what types of defendants can be sued. A number of jurisdictions, especially in the civil law world, envision such suits to be initiated in the shareholder meeting. Part 2.3 looks at this type of suit. Part 2.4 looks at the more important type of litigation, namely derivative suits in the proper sense, which are initiated by minority shareholders directly and exist in all nine jurisdictions. Part 2.5 briefly looks at information-gathering mechanisms that help plaintiffs to meet their burden of proof, which is a considerable hurdle in some jurisdictions. Part 2.6 concludes.

## 2.2. Derivative litigation systems: Suitable defendants and admissible types of claims

### 2.2.1. Flexible derivative litigation systems in common law countries

In terms of the type of instrument covered by this chapter, we look at instruments designed to remedy reflective loss where shareholders are harmed only by the loss of value of their interest in the corporation. In other words, we look at lawsuits initiated by stockholders that seek to reimburse the corporation for injury inflicted on it, rather than in shareholders directly.<sup>28</sup> In most jurisdictions the distinction to other types of suits is relatively clear and depends on the plaintiff's actual application for relief.<sup>29</sup> In the UK and other Commonwealth jurisdictions courts sometimes use oppression actions (a flexible instrument for the benefit of minority shareholders with a wide variety of possible remedies) to order relief to the corporation, even if this is not its main purpose.<sup>30</sup> The chapter omits these and focuses on instruments specifically designed to address reflective loss.

In the common law world, the US derivative stands out as an influential model, much of which is governed by tradition and case law. Under **US** law, in principle anyone can be sued derivatively. As Robert Clark explains, a derivative suit has historically had two parts. "The plaintiff (1) brought a suit in equity against the corporation seeking an order compelling it (2) to bring a suit for damages or other relief against some third person who had caused legal injury to the corporation." While the defendant is "usually an officer, director or other fiduciary of the corporation," this is not a legal requirement.<sup>31</sup> Consequently, "[a]ny claim belonging to the corporation may, in appropriate circumstances, be asserted in a derivative action, including claims that do – and claims that do not—involve corporate mismanagement or breach of fiduciary duty."<sup>32</sup> Derivative suits are often not only brought against directors and officers, but also against controlling shareholders. Derivative suits can be brought to claim damages, but also to seek an injunction prohibiting or compelling certain conduct by directors.<sup>33</sup>

The law is similarly broad in **Singapore** and **Israel**, where derivative suits have a clear basis in legislation. **Singapore's** law is peculiar in that there are two separate mechanisms that apply in parallel – one developed in the common law (and historically based on the UK law), and one established by statute.<sup>34</sup> The statutory regime of ss. 216A and 216B was originally modelled on Canadian law in 1993 and excluded firms listed on the Singapore Exchange and foreign incorporated companies.<sup>35</sup> This restriction on listed companies (but not foreign incorporated companies) was removed only in 2014.<sup>36</sup> In this point, it differs from the **UK**, where the Companies Act of 2006 has superseded the traditional model.<sup>37</sup> While prior to 2014 **Singapore** plaintiffs in listed companies and foreign incorporated corporations had to use the common law – which set up considerable obstacles under the ancient English precedent of *Foss v. Harbottle*<sup>38</sup> – the reform makes the common law action less significant as now only foreign incorporated corporations are limited to the common law. Consequently, this chapter therefore only discusses the statutory action.<sup>39</sup>

In terms of suitable defendants, there are cases where derivative suits are brought against other shareholders of the corporation.<sup>40</sup> The **Singapore** Companies Act's definition of a derivative suit is a situation where a shareholder brings "an action or arbitration in the name and on behalf of the company" or intervenes in such an action<sup>41</sup> without specifying the type of defendant.<sup>42</sup> The forms of corporate relief granted by the statutory law are not limited to damages suffered by the company but may also assume the right (i) to bring an action/arbitration, or (ii) to intervene in an action/arbitration to which the company is a party for the purpose of prosecuting, defending or discontinuing the arbitration/action on the company's behalf.<sup>43</sup>

In **Israel**, the law does not specify the types of defendants in a derivative suit, or the type of remedy available.<sup>44</sup> The fact that the law provides for a derivative defence – where a shareholder can ask for leave to defend a claim on behalf of the corporation – supports that any claim should be permissible.<sup>45</sup>

The least flexible regime among the four common law countries in this respect seems to be that of the **UK**, which (like the civil law countries' discussed below) focuses on claims against directors.<sup>46</sup> Section 260(3) of the Companies Act provides that "a derivative action may only be brought in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director, former director or shadow director of the company."<sup>47</sup> However, s. 260 of the Companies Act can be used "against the director or another person (third party) or both."<sup>48</sup> A "shadow director" is a person "in accordance with whose directions or instructions the directors of the company are accustomed to act."<sup>49</sup> Under certain circumstances, this can include controlling shareholders; however, under the Companies Act 2006, a "body corporate" cannot qualify as a shadow director for purposes of general directors' duties "by reason only that the directors of the subsidiary are accustomed to act in accordance with its directions or instructions."<sup>50</sup> Moreover, UK courts have also developed the concept of "de facto directors", who are individuals acting as directors without being formally appointed.<sup>51</sup> Consequently, directors' duties apply to them as well. While controlling shareholders are potentially at risk as being classified as shadow directors, exercising voting powers or nominating directors does not make that shareholder a shadow director.<sup>52</sup> Besides shadow and de facto directors, the case law supports that stockholders can bring a derivative claim against a person dishonestly assisting a director in a breach of duty, or against someone who knowingly receives property from a director's breach.<sup>53</sup>

The UK statute appears not to specify the type of remedy<sup>54</sup>, although traditionally it has been used for damages claims. As a matter of fact, s. 260(2)(b) allows the enforcement of court orders under s. 994 ("unfair prejudice"), which is a flexible remedy which can be brought e.g. against a majority shareholder acting oppressively. It is certain that the unfair prejudice remedy can be used to ask for an injunction as outlined in s. 996.<sup>55</sup> The disadvantage is that, unlike in a derivative suit, the company does not have to indemnify the plaintiff.<sup>56</sup>

### 2.2.2. Analogous mechanisms to enforce directors' duties in civil law countries

By contrast, the five civil law countries are more restrictive in the capabilities of derivative suits. Their legal regimes are clearly special statutory regime for the enforcement of liability for violations of directors' duties. This means that defendants are (with exceptions) only board members, and that claims are limited to liability. Thus, as a baseline *only members of the managing or (sometimes) supervising body of the company* can be sued in **France**<sup>57</sup>, **Germany**<sup>58</sup>, **Italy**<sup>59</sup> and **Spain**<sup>60</sup>. The precise roles functionaries that are suitable defendants depends on the corporate governance structure. For example, in **Germany**, where the two-tier system prevails, both members of the supervisory board (*Aufsichtsrat*) and members of the management board (*Vorstand*) can be sued. In **Spain**, the members of the board of directors (*administradores*) are suitable defendants.

France and Italy allow firms to choose different between board structures. In **Italy**, when a firm has the traditional structure with a board of directors and a board of auditors, both members of the board of directors (*amministratori*) and of the board of statutory auditors (*sindaci*) are suitable defendants.<sup>61</sup> In firms with the dualistic model, these provisions apply to the members of the management and supervisory boards, and in the unitary or one-tier system to the board members and audit committee members.<sup>62</sup> In **France's** (more common) one-tier structure, only the *administrateurs* (board members) and the *Directeur général* (CEO) are suitable defendants in the derivative suit mechanism governed by the Commercial Code (*action sociale ut singuli*).<sup>63</sup> So-called *directeurs généraux délégués* (senior officers with similar functions as the CEO)<sup>64</sup> cannot be sued under the Commercial Code unless they are also members of the management board, but they can be sued under a similar derivative suit mechanism under a general provision of the civil law applicable to all business associations.<sup>65</sup> The disadvantage is that shareholders then must sue individually and cannot sue jointly (which has some advantages for litigation cost).<sup>66</sup> In the two-tier model, the (*directoire*) or the *directeur général*, if the management board as only one member, are suitable defendants.<sup>67</sup> Members of the supervisory board can only be sued for their own fault in the exercise of their oversight function, but not for management mistakes since the supervisory board is not allowed to take management decisions.<sup>68</sup> Shareholders can also bring derivative suits against former members of company bodies.<sup>69</sup> Similarly, in **Brazil**<sup>70</sup>, whose board structure resembles the traditional one in France, both officers (*diretores*), members of the board (*conselheiros de administração*) and also a third party who allegedly assists in the wrongdoing are suitable defendants.

Under these legal regimes, it is often more difficult to sue other defendants such as **controlling shareholders** than in the US. For example, **French** courts have explicitly rejected that an "*action sociale ut singuli*" can be brought against a third party such as a controlling shareholder in most circumstances.<sup>71</sup> In **Brazil**, **Germany** and **Italy**, there are special litigation mechanisms for lawsuits brought in the context of corporate groups.<sup>72</sup> These countries have a specific legal regime that applies when a company is integrated into a corporate group. A "controlling enterprise" under these rules may be subject to liability that can be enforced by minority shareholders of the subsidiary. However, in the case of **Germany** and **Italy**, the defendant in this case must itself be a corporation or other legal entity and cannot be an individual.<sup>73</sup> In the case of **Brazil**, article 246 of the Company Law literally states that the defendant must itself be a legal entity, but some legal scholars have defended that the only possible interpretation of the law is that article 246 is applicable both to controlling entities and to controlling private individuals.<sup>74</sup> Interestingly, in **Italy** this type of lawsuit is a *direct* and not a derivative suit. In other words, shareholders (or creditors) would claim liability from the controlling entity for themselves and not for the corporation. This chapter therefore covers the German mechanism, but not the Italian one.

Individuals who are not members of corporate bodies can under certain circumstances still be liable even such a mechanism does not apply or exist. In **Spain**, the derivative suit mechanism explicitly applies to *de facto directors* as well. This term refers to "persons who perform the tasks and role of director without the title, or with a null or void title, or with another title."<sup>75</sup> In addition, the liability regime and enforcement

mechanism apply to the person who has been delegated as the highest management authority within the company (i.e. if that person is not a director).<sup>76</sup>

In **France**, courts have allowed shareholder derivative action against accomplices of director in criminal case involving the misappropriation of corporate assets (*abus de biens sociaux*).<sup>77</sup> Even without a statutory basis, there has been a debate whether the derivative suit mechanism applies to so-called *dirigeants de fait* (de facto directors).<sup>78</sup> In 2016 and 2017, in two decisions concerning the same case, the *Cour de Cassation* allowed shareholders to sue de facto directors, specifically against another firm that controlled the entity in question.<sup>79</sup> However, because the Commercial Code does not mention de facto directors, the litigation mechanism of the *action sociale ut singuli* (derivative suit) does not apply. Instead, minority shareholders must ask the court to appoint a special representative (*mandataire ad hoc*) to enforce the claim.<sup>80</sup> In any event, the bar for a controlling shareholder to qualify as a de facto director is relatively high and requires a sustained interference with the central governance functions of the corporation.<sup>81</sup> Likewise, **Italian** law has over time developed the concept of the *amministratore di fatto* (de facto director), although it is not entirely clear when a parent company can qualify as such.<sup>82</sup>

In all of these **jurisdictions**, the derivative suit mechanism only serves the purpose of enforcing **damages claims** of the company resulting from violations of directors' duties.<sup>83</sup> Consequently, it is not used to enjoin transactions harming the interests of minority shareholders. This does not necessarily mean that shareholders never have recourse against such transactions. In particular, when a transaction requires a shareholder vote, minority shareholders may be able to bring a rescission suit against a decision endorsed by the majority.<sup>84</sup> In some jurisdiction, shareholders may also be able sue to void board resolutions.<sup>85</sup> However, there are likely certain transactions where shareholders have little or no recourse.

### 2.2.3. Assessment and issues for discussion

As we have seen, jurisdictions differ as to whether derivative litigation mechanisms can be used for any claim and for any type of remedy (as in the **US, Israel and Singapore**), or whether they can be used only to enforce monetary liability of directors and other members of corporate bodies (as in the other jurisdictions). From the perspective of holding controlling shareholders accountable, e.g. for self-dealing transactions, it seems at first glance advantageous to implement a mechanism with an open purpose. Otherwise, shareholders may sue directors/and officers, but this will typically not be a great help if the director does not have the means to compensate shareholders (e.g. for a large self-dealing transaction).

Shareholders should also be able to use the derivative suit mechanism to bring an injunction, as is permitted e.g. in the US. An injunction can serve the purpose of stopping a harmful self-dealing transaction in which the controlling shareholder is engaged. However, in the larger context, there are some contextual factors to consider.

- First, are there other effective mechanisms that allow shareholders to block transactions harming the company? For example, other types of lawsuits that take over the function of derivative suits, e.g. class actions? In addition, if a broad set of transactions require a decision of the shareholder meeting, shareholders may challenge such transactions by seeking to have the right to rescind such decisions, and they may have an individual right to enjoin such transactions if no vote takes place. (This assumes, of course, that there are effective ways for shareholders to learn of plans for such transactions).
- Second, to what extent does injunctive relief increase the power of “professional plaintiffs” seeking payment from the corporation in exchange for dropping the suit?
- Third, are derivative suits advantageous relative to other actions, such as class actions or unfair prejudice actions? Whether a particular mechanism is attractive for potential plaintiffs will depend on which financial risks are involved, and who must pay for the cost of litigation if it is not successful (See more on this below Section 2.4.6).

- Fourth, derivative suits cannot be seen completely in isolation from the underlying substantive law. Whether we are likely to see many derivative suits depends in part on the substantive law, and what elements of a claim plaintiffs must prove. For example, in Delaware firms can opt out of directors' liability for violations of the duty of care,<sup>86</sup> which means that derivative suits for such violations will typically only be brought for the purpose of obtaining an injunction.

Table 2.1. Overview of derivative litigation systems (Part 2)

Country	Brazil	France	Germany	Israel	Italy	Singapore	Spain	UK	USA
Defendants	Management, supervisory board members and other participants	Management board members, CEO, accomplices; de facto directors under civil law	Management and supervisory board members; controlling enterprise (corporate group law)	Anyone	Board members and audit board members; controlling enterprise (corporate group law – direct suit)	Anyone	Directors, de facto directors, CEO	Anyone	Anyone
Types of claims	Damages for violations of directors' duties and abuse of controlling power	Damages for violations of directors' duties	Damages for violation of directors' duties (damages for violations of controlling enterprise's duties)	Any claim; in addition, allows a "derivative defence" (infra section 2.4.5)	Damages for violation of directors' duties	Any claim, including intervention in arbitration proceedings	Damages for violation of directors' duties	Causes of action arising from violation of directors' duties involving negligence, default, breach of duty or breach of trust	Any claim

## 2.3. Suits initiated in the shareholder meeting

### 2.3.1. Countries that do not involve the shareholder meeting in derivative suits

Several jurisdictions involve the shareholder meeting in decisions to pursue liability claims against directors, but there are considerable differences across countries. The majority of countries do not involve the shareholder meeting in the decision. **UK** law and **Israeli** law make no mention of it.<sup>87</sup> Neither does the law of **Singapore**, although there is at least one case where the plaintiff brought the issue to the other shareholders in the meeting, and pursued a derivative suit after being rejected in an extraordinary shareholder meeting.<sup>88</sup> However, one could argue that the **UK** indirectly involves shareholders by allowing the *ratification* of directors' actions that would otherwise be breaches of duty.<sup>89</sup> By contrast, in **Singapore**, an approval of an alleged breach by a majority of members does not necessarily lead to the action's dismissal.<sup>90</sup>

In **Delaware**, there is presently *no* requirement that plaintiffs must first bring their grievance to their fellow shareholders and obtain their consent to a suit. Such a requirement existed in the past and was abolished in 1968.<sup>91</sup> By contrast, "demand" on the board is very important (See below Section 2.4.4). However, at present 21 states of the **US** still have such a requirement on the books.<sup>92</sup> When a derivative action is brought in federal court, the Federal Rules of Civil Procedure<sup>93</sup> defer to the applicable state law as to whether demand on shareholders is necessary.<sup>94</sup> Historically, the Delaware courts excused demand on shareholders when the wrongs could not be ratified by majority shareholders (because they were ultra

vires, illegal, or fraudulent).<sup>95</sup> Even states that still require demand on shareholders, typically allow minority shareholders to go forward with a suit if a (conflicted) majority shareholder rejects the demand.<sup>96</sup> Often demand on shareholders is excused because it would be impracticable in a corporation with a large number of stockholders.<sup>97</sup>

Among civil law countries, **France** prohibits any clause in the article that would require the shareholder meeting to approve a derivative suit or that would waive the right of shareholders to bring such a suit.<sup>98</sup>

### **2.3.2. Countries that (sometimes) involve the shareholder meeting in enforcing directors' liability**

#### *2.3.2.1 Putting suits against directors on the agenda*

**Brazil**<sup>99</sup>, **Germany**<sup>100</sup>, **Italy**<sup>101</sup> and **Spain**<sup>102</sup> explicitly allow shareholders to vote on bringing a lawsuit enforcing the liability of members of corporate bodies. Often the chance of obtaining a majority is slim, given that the majority shareholder selected the directors or may even be involved in the conduct that gave rise to the alleged course of action. In **Brazil** and in **Spain**, shareholders must first bring the issue to the shareholder meeting unless – exclusively in the later jurisdiction – the allegation involves a breach of the duty of loyalty.<sup>103</sup> This contrasts with **German** and **Italian** law, which do not **require** going to the meeting prior to pursuing a derivative action individually.

A major difficulty is often the addition of an item regarding litigation on the shareholder meeting's agenda. Typically, the shareholder meeting can only pass resolutions that have officially been announced in the agenda. Agenda-setting is particularly difficult in **Germany** even if there is an upcoming meeting because normal rules regarding putting items on the agenda apply.<sup>104</sup> Thus, a minority of shareholder holding at least 5% or EUR 500,000 of the firm's capital can request that an item be put on the agenda.<sup>105</sup> According to legal scholars, individual shareholders can still request a vote if it closely relates to another agenda item, in particular the presentation of a special report investigating malfeasance; the announcement of a vote on the "discharge" of corporate bodies (which happens routinely every year) does not suffice.<sup>106</sup>

**Spanish** law is permissive in stating a resolution on liability can be passed upon the request of any shareholder even if it was *not* on the meeting's agenda.<sup>107</sup> Similarly, in **Brazil**<sup>108</sup> and in **Italy**<sup>109</sup> a resolution can be passed in any annual general meeting without a specific agenda item (in Italy it must be in the context of the discussion of the firm's financial statements). In the three countries, if there is no upcoming meeting, a minority of shareholders holding 5% of the company's capital may convene a general meeting.<sup>110</sup> In listed companies in **Brazil**, the percentage is reduced depending on the amount of the outstanding capital stock (the bigger the capital stock, the smaller the ownership requirement).<sup>111</sup> In listed companies in **Spain**, the percentage is reduced to 3%.<sup>112</sup> In **Italian** listed companies, a minority of 2.5% may use a special procedure under the capital markets law to put items on the agenda.<sup>113</sup>

#### *2.3.2.2. Voting on the liability suit*

Once the item is on the agenda, it must be approved with a majority of the votes present or represented in the meeting.<sup>114</sup> **Spanish** law explicitly states that the corporation's articles cannot require a higher majority,<sup>115</sup> whereas in **Brazil** such a prohibition exists only in listed companies.<sup>116</sup> In **Germany** this is not explicitly stated, but the result of the prevailing scholarly interpretation.<sup>117</sup>

In **Brazil**, **Germany** and **Italy**, directors against whom liability is to be enforced are barred from voting on the decision.<sup>118</sup> According to a decision of the German supreme court, the same is true for shareholders who were involved in the director's breach of duty.<sup>119</sup> According to commentators in the German legal literature, a shareholder may also be precluded from voting when a board member (who is to be sued) has a significant influence of the shareholder's vote.<sup>120</sup> Shareholders who merely voted in favour of a particular director are not excluded from voting on the enforcement of claims against that person. In **Spain**, directors



are not allowed to vote on decisions relieving them of the duty of loyalty.<sup>121</sup> This provision might also be used to argue that they cannot vote on liability claims at least in some circumstances. In the **UK**, where shareholders can ratify breaches of directors' duties, neither the director in question nor any members of the company connected to him may vote.<sup>122</sup>

### 2.3.2.3. Representation of the company

If the vote succeeds, the task of bringing the suit devolves to the corporate bodies who are obligated to pursue the claims.<sup>123</sup> Normally, this will mean that the board represents the corporation. However, clearly this involves a conflict of interest if current members are to be sued. Under **Germany's** two-tier board structure, the management board would normally represent the corporation; if the defendant would be management board members, this task devolves to the supervisory board.<sup>124</sup> Obviously, this solution is not perfect, given that members of both boards are often close or members of both may be sued. **Brazil** and **Spain** have an entirely different solution: the decision to proceed with a liability action automatically entails the director's removal.<sup>125</sup> This would seem to eliminate the most pressing conflict of interest and allow new directors to enforce the claim, although it by no means guarantees vigorous enforcement. The same is true in **Italy**, but only if the resolution to sue passed with at least with the support of shareholders representing 20% of the company's capital; the shareholders must then vote on replacements.<sup>126</sup>

In **Brazil** and in **Spain**, the company must pursue a suit within a period specified by law (three months in the first case and one month in the later jurisdiction); otherwise (or if the majority votes against it), minority shareholders' can pursue the suit themselves.<sup>127</sup> **Germany** requires that the responsible corporate body must pursue a suit within 6 months.<sup>128</sup>

To deal with potential conflicts of interest, in **Germany** shareholders may vote (with a majority) to appoint a special representative to pursue such claims.<sup>129</sup> A minority holding at least 10% or EUR 1 000 000 of the company's capital can petition the court to appoint such a special representative (which the court may do if it finds this to be appropriate given the circumstances).<sup>130</sup> In **Italy**, the court *must* appoint a special representative to act on behalf of the corporation if the defendant directors (who would otherwise be responsible for bringing the suit) are still in office and are therefore subject to a conflict of interest.<sup>131</sup>

The current board members may be inclined to settle the claim against former board members because they have come to the conclusion that the suit is not meritorious, or for less benign reasons. A *settlement* (or waiver) of the claim therefore requires a vote in the shareholder meeting in all three **European** countries, while the **Brazilian** Company Law does not have any provision regarding the requirements for settling or waiving the claim.<sup>132</sup> However, the law in the three European countries specifies a percentage of shareholders that must not object to such a decision (10% in Germany, 5% in publicly traded firms and 20% in other firms in **Italy**, 3% in publicly traded firms and 5% otherwise in **Spain**).<sup>133</sup>

### 2.3.2.4. Cost of the proceedings

The corporation in its capacity as plaintiff is responsible for the cost of pursuing the suit (regardless of whether it is represented by a corporate body or a special representative).<sup>134</sup> Court fees for a contestable petition to appoint a special representative in **Germany** are borne by the corporation if the petition is successful.<sup>135</sup> Consequently, shareholders themselves normally have the burden of all other costs, as well as with court fees if the petition is not successful.<sup>136</sup>

### 2.3.3. Assessment and issues for discussion

Mechanisms involving the shareholder meeting, such as the ones discussed in this part, tend not to be frequently used to enforce directors' liability. First, the relatively high percentage thresholds may be difficult to surmount for disgruntled minority shareholders. Second, the process to initiate litigation is cumbersome and likely results in valuable time being lost. Minority shareholders must add an item to the shareholder

agenda, and then persuade the majority to vote in favour of the suit (**Germany** is the only of the three countries that gives a qualified minority the right to ask the court to appoint a special representative). Third, voting prohibitions cover only defendants themselves, but not other shareholders who supported the defendants. Thus, it is typically difficult to put together a majority in favour of the suit. Fourth, it is typically not attractive for shareholders to lose control over a suit to hand it over to (new) directors or a special representative that may not pursue the claim in accordance with their preferences. Thus, minority shareholders are more likely to use the actual derivative litigation mechanisms discussed in Section 2.4, where they are typically able to retain control.

Table 2.2. Litigation mechanisms involving the shareholder meeting (Part 3)

Country	Brazil	France	Germany	Israel	Italy	Singapore	Spain	UK	USA
Involvement of shareholder meeting	Required	No.	Optional	No.	Optional	No.	Required unless allegation of breach of duty of loyalty	No, but shareholders can ratify breaches.	No (Delaware)
Lawsuit must be on shareholder meeting's agenda	Vote can be passed in any AGM (but must be in the agenda in extraordinary general meetings)	N/A	Normally need capital share of 5% or EUR 500,000	N/A	Vote can be passed in AGM when discussing financial statements.	N/A	Vote can be requested by any shareholder even if not on agenda. (5% to call special meeting, 3% in listed company)	N/A	N/A
Majority meeting in for lawsuit	Majority, cannot be modified for listed companies	N/A	Majority, cannot be modified	N/A	Majority [of social capital if in extraordinary meeting, which statutes can increase]	N/A	Majority, cannot be modified	N/A	N/A
Voting prohibition for defendants?	Yes	N/A	Yes	N/A	Yes	N/A	Possibly, if decision relieves them of duty of loyalty	Yes, including members connected to director.	N/A
Defendants stay in office?	No	N/A	Yes	N/A	No, if decision is made with at least 20% of share capital.	N/A	No	N/A	N/A
Special representative to represent company	N/A	N/A	Yes, if appointed by shareholder meeting; court can appoint upon request of 10% / EUR 1 000 000	N/A	Yes, if defendant directors are still in office.	N/A	No	N/A	N/A

Country	Brazil	France	Germany	Israel	Italy	Singapore	Spain	UK	USA
Company can settle?	Not addressed in the law	N/A	Yes, requires shareholder vote to which 10% of capital can object	N/A	Yes, requires shareholder vote to which 5% (20% if privately held) of capital can object	N/A	Yes, requires shareholder vote to which 5% of capital object (3% in listed company) can object	N/A	N/A

## 2.4. Suits initiated by (minority) shareholders

### 2.4.1. Overview

All nine jurisdictions permit lawsuits in which individual shareholders or groups of shareholders represent the corporation under certain circumstances. In these cases, plaintiff shareholders (and their attorneys) represent the corporation, while the beneficiary of the remedy is the corporation. These suits are accurately described as **derivative suits** in the proper sense.

A threshold question is whether shareholders need to go through certain steps to take the corporations into their own hands and bypass other corporate bodies. For example, in the **US**, Delaware law provides that “[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation. [...]”.<sup>137</sup> Derivative suits are intended as an exception to this principle, which is why plaintiffs sometimes have to fulfil certain requirements that do not exist in civil procedure in general.

Even in jurisdictions that allow shareholder convening in a meeting to collectively enforce claims against directors (Brazil, Germany, Italy, and Spain)<sup>138</sup> only **Brazil** and **Spain** require a prior involvement of the shareholder meeting in most cases. However, even in Spain an exception is made when the allegation involves a violation of the duty of loyalty. Otherwise, in Spain shareholders can sue to “defend corporate interests when the directors fail to convene the general meeting requested for these purposes, when the company does not bring said action within one month of the date of the adoption of the respective resolution, or when the meeting decides against the claim for liability.”<sup>139</sup>

Most countries provide only one mechanism for derivative litigation, with two exceptions. First, as mentioned above in Section 2.2.1, in **Singapore**, in limited circumstances, the common law derivative suit applies in parallel to the statutory regime. This chapter discusses only the latter. Second, **Germany** provides two types of derivative suits.<sup>140</sup> The first is a procedure to enforce directors’ liability claims, which has applies to all public limited companies (*Aktiengesellschaften*).<sup>141</sup> The second procedure is part of the law on corporate groups.<sup>142</sup> This section also allows a true derivative suit controlled by a shareholder, but it applies only in a limited context, specifically when a controlling business entity induces a subsidiary corporation to enter into disadvantageous transactions without compensating it within the business year.<sup>143</sup> The more broadly applicable procedure to enforce director’s liability uses a pre-trial “lawsuit admission procedure” with some similarities to US law, which has the advantage that it limits the exposure of minority shareholders to the risk of litigation cost. By contrast, the corporate group action has less developed procedural rules and provides for no preliminary procedure. This is likely the reason why it has attained little practical significance. This chapter discusses both types of suits.

### 2.4.2. Suitable shareholder plaintiffs, minimum ownership thresholds and the selection among competing shareholders

In the **US**, the corporation for which a remedy is sought is represented by an individual shareholder acting on its behalf.<sup>144</sup> While the Delaware Chancery Court's rules do not have an explicit requirement of adequacy, the Federal Rules of Civil Procedure (as well many state statutes and rules), requires that the plaintiff must "fairly and adequately represent the interests of shareholders."<sup>145</sup> In practice, this almost never screens out lawsuits.

The other jurisdictions do not have comparable requirements. However, **Brazil, Germany, Italy and Spain** require *minimum ownership thresholds* of shares to have standing. In **Brazil**, the current threshold is 5% of the equity for privately-held companies and, for listed companies, the ownership requirement is further reduced depending on the amount of outstanding capital stock of the company.<sup>146</sup> In **Germany**, the cut-off is a capital share of 1% or EUR 100,000.<sup>147</sup> In both countries, there is no minimum ownership requirement for the special derivative suit against the controlling enterprise under the law of corporate groups.<sup>148</sup> Additionally, in **Brazil** any individual **shareholder** can sue if the company fails to file a lawsuit requested by the shareholders' meeting within three months.<sup>149</sup> In **Italy** the threshold is 2.5% for publicly traded firms and 20% in others; the articles can modify this threshold, although in publicly traded firms they can only reduce it.<sup>150</sup> In **Spain**, the threshold is the one necessary to call a general meeting, namely 5% (or lower if stipulated in the articles).<sup>151</sup> The amount is reduced to 3% in publicly traded firms.<sup>152</sup>

The theory behind minimum ownership thresholds is that they serve to screen out abusive lawsuits: Likely the benefit to a small shareholder for a derivative suit is extremely small, which is why such a person is unlikely to sue for a legitimate reason.<sup>153</sup> In this respect, the purpose functionally corresponds to the US "fair and adequate representation" standard. Even though multiple shareholders can act jointly to meet the threshold, this cut-off mechanism makes derivative suits very difficult.

The **US**, the **UK**<sup>154</sup>, **Singapore**<sup>155</sup>, **Israel**<sup>156</sup> and **France** allow shareholders to sue individually without regard to their ownership stake.<sup>157</sup> However, in **France**, the creation of a group of shareholders has certain procedural advantages. In this case, shareholders must unanimously appoint a representative (or representatives).<sup>158</sup> To create a group, shareholders must hold 5% of the outstanding shares.<sup>159</sup> The minimum amount is reduced if the company's capital exceeds EUR 750,000. In this case, the percentage is computed by summing up the follow percentages for each bracket of capital:<sup>160</sup>

Table 2.3. Minimum percentages required for plaintiff groups in France

	Percentage
For the first EUR 750 000	4%
For the bracket from EUR 750 000 to EUR 7 500 000	2.5%
For the bracket from EUR 7 500,000 to EUR 15 000 000	1%
For all capital above EUR 15 000 000	0.5%

Instead of an *ad hoc association*, shareholders of a publicly traded may also establish an association to represent their interests (*groupement de défense*), which must deposit its articles with the **French** securities regulator (AMF). In this case, a slightly different minimum ownership thresholds apply.<sup>161</sup>

If there are multiple competing plaintiffs, the **Delaware** courts use a variety of criteria to determine who should be the lead plaintiff. These include the quality of the pleadings, the relative economic stakes of the competing litigants, the willingness and ability of all the contestants to litigate vigorously on behalf of an entire class of shareholders, the absence of any conflict between larger and smaller stockholders, the enthusiasm or vigour with which the various contestants have prosecuted the lawsuit, as well as the competence of counsel and their access to the resources necessary to prosecute the claims.<sup>162</sup> There is no presumption of favour of the largest plaintiff,<sup>163</sup> or in favour of the first to file a suit.<sup>164</sup>

### 2.4.3. Contemporaneous and continuous ownership of stock

Some jurisdictions require shareholders to have held shares at a particular point in time to serve as eligible plaintiffs. In the **United States**, under the so-called “contemporaneous ownership requirement” plaintiffs or their predecessors<sup>165</sup> must have been stockholders *at the time of the alleged wrongful act or omission*.<sup>166</sup> Similarly, in **Germany** plaintiffs or their predecessor must have held shares before learning about the alleged breach.<sup>167</sup> By contrast, **UK** law says explicitly that it is immaterial whether the cause of action before or after the plaintiff became a member.<sup>168</sup> Former members cannot sue.<sup>169</sup> None of the other jurisdictions have explicitly adopted a requirement of this type. Typically, statutory language permitting any shareholder to bring a suit indicate that prior ownership is not necessary.<sup>170</sup> **Italy** has historically required that shareholders must have held their stock for at least 6 months before the suit, but this provision was repealed in 2003.<sup>171</sup>

In the **US**, plaintiffs must hold on to their shares for the duration of the lawsuit (“continuous ownership requirement”), which follows from the requirement that the plaintiff must fairly and adequately represent the interests of shareholders.<sup>172</sup> The other jurisdictions do not have such requirements, although at least in **Germany**<sup>173</sup> and **Israel**<sup>174</sup> there are academic debates about the issue. In **Italy**, the code of civil procedure provides that a trial continues with the original parties in the case of an *inter vivos* transfer.<sup>175</sup> In **France**, in the related issue of proceedings to appoint an independent expert to assess a management decision, according to a 2005 case, share ownership at the time of the application sufficed, and subsequent cancellation of these shares did not affect the applicant’s standing.<sup>176</sup>

### 2.4.4. Pre-trial procedures

#### 2.4.4.1. Requirement of a judicial pre-trial procedure

In addition to standing requirements, many jurisdictions have created a pre-trial or first stage procedure to decide about the admission of a derivative suit. The basic reason for this is the fact that the decision to bring a lawsuit on the behalf of a corporation would normally rest with the board of directors or another decision-making body within the company. Derivative suits where shareholders take this power from the board must therefore undergo special scrutiny. Pre-trial procedures serve the important function in screening out non-meritorious lawsuits and plaintiffs. In the **United States**, this is particularly significant because only after a derivative suit has passed the “demand” stage, plaintiffs will be granted discovery (see below Section 2.5), which is their best shot at obtaining evidence to substantiate the suit. Because plaintiffs rarely make demand and normally go to court claiming demand futility (See below Section 2.4.4), the decision to admit the suit lies essentially with the court. In this respect, **Delaware** is in effect similar to **UK** or **Singapore** law, where plaintiffs must ask for the court’s permission or “leave” to bring a derivative claim.<sup>177</sup>

In other jurisdictions, a preliminary screening procedure often has the effect of limiting the plaintiff’s exposure to financial litigation risk. Success in a preliminary procedure can serve as a cut-off point after which the corporation (for whose benefit the derivative suit is brought) must bear litigation cost. Court fees that a shareholder plaintiff will have to advance, or security for litigation expenses a plaintiff have to provide may be limited to the smaller amount at stake in the pre-trial procedure. Thus, financial incentives against the pursuit of such suits by smaller shareholders may be limited. This is particularly apparent in jurisdictions without any pre-trial stage, such as **Brazil**, **Italy**<sup>178</sup>, **France**<sup>179</sup> or **Spain**<sup>180</sup>, but also the **German law of corporate groups**.<sup>181</sup> In spite of the seemingly simple procedure, derivative suits by minority shareholders are not common under these legal regimes. Part of the explanation is likely that plaintiffs are exposed to the full financial litigation risk.

#### 2.4.4.2. Demand requirements and the corporation's response

In the **US**, **Germany** (in suits regarding directors' liability), **Israel** and **Singapore** (but not in the **UK**), shareholders at least in theory first must ask the company's board to litigate the claim in question before initiating a pre-trial procedure in court. Plaintiffs usually do not favour such a requirement because it gives the board the opportunity to further stall the suit. In the **US**, this is known as the "demand requirement." Procedural rules in **Delaware** require that the "complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff's failure to obtain the action or for not making the effort."<sup>182</sup> In **Singapore**, demand must be made on the directors. In **Germany**, plaintiffs must request that the corporation sue, whereas **Israeli** law specifies that the demand must give reasons and be in writing, and it must be addressed to the chairman of the board.<sup>183</sup> Unlike in Delaware, in none of these other jurisdictions does the rejection of the demand hinder the lawsuit (see *infra* Section 2.4.4).

In practice, in **Delaware** plaintiff shareholders only rarely make demand largely because the way in which the courts will subsequently analyse conflicts of interest of directors makes it nearly impossible for them to proceed with the derivative suit after actually making demand.<sup>184</sup> This "rule of universal non-demand" contrasts with the **Revised Model Business Corporation Act** (RMBCA), which requires that shareholders always must make written demand on the board and wait for 90 days before suing in court.<sup>185</sup> It also differs from the three non-US jurisdictions requirement demand: **Israeli** law requires a response from the company within 45 days.<sup>186</sup> The company can either take an action or reach a decision which results in the elimination of the cause of action brought forward by the plaintiff, reject the plaintiff's demand providing reasons for that decision, or bring the action.<sup>187</sup> The response must set out in detail the action taken, name the participants in the decision, and disclose their conflicts of if any participant in the decision or office holder of the company had a personal interest in the decision.<sup>188</sup> In **Singapore**, the complainant must have "given 14 days' notice to the directors of the company of his intention to apply to the Court" "if the directors of the company do not bring, diligently prosecute or defend or discontinue the action or arbitration."<sup>189</sup> In some circumstances, the court has discretion to grant leave to the complainant to pursue a derivative action even when the formal notice requirements have not been satisfied.<sup>190</sup> In **Germany**, the law only says that plaintiffs must show that have given the corporation a reasonable amount of time to bring a suit.<sup>191</sup>

#### 2.4.4.3. Criteria for the court's decision

All five jurisdictions with a pre-trial procedure require a court decision as to whether a derivative suit can proceed. In **Delaware**, because plaintiffs typically do not make demand, the court will take this decision when deciding about demand futility (i.e. whether it would have been futile for plaintiff shareholders to make demand). The four jurisdictions differ as to whether the court's decision turns on the directors' conflicts of interest (**Delaware**), on whether the suit is likely in the best interests of the corporation (**Germany**, **Singapore**, **UK**), or both issues (**Israel**). In **Israel**, **Singapore** and the **UK**, the court additionally must assess the plaintiffs' motives (good faith).

In the **US**, the **Delaware** Supreme Court has established a two-part test for demand futility.<sup>192</sup> In their pleadings, plaintiffs must establish "(1) whether threshold presumptions of director disinterest or independence are rebutted by well-pleaded facts; and, if not, (2) whether the complaint pleads particularized facts sufficient to create a reasonable doubt that the challenged transaction was the product of a valid exercise of business judgment."<sup>193</sup>

It suffices for plaintiffs to show only one of them. The plaintiff can show an absence of disinterestedness in making the decision about the lawsuit (first alternative). Even if the board appears disinterested, demand will be excused if the plaintiff is able to plead facts "that the challenged transaction is so egregious on its face as to flunk the business judgment rule and thereby leave the directors who approved the transaction facing liability for breaching their duty of care" (second alternative).<sup>194</sup> In some cases, plaintiffs cannot rely

on the second alternative of the demand futility test. This is the case when it was not the current board of the corporation that approved the transaction challenged in the derivative suit.<sup>195</sup> Consequently, e.g. in a double derivative suit (when the shareholder of a subsidiary seeks to compel the enforcement of a claim of a parent company), when board members have changed, or when attempting to enforce a claim against corporate officers, the first alternative of the test is their only option.

In spite of the principle that plaintiffs should make demand, they are in practice ill-advised to do so in Delaware because the court found that “[b]y electing to make a demand, a shareholder plaintiff tacitly concedes the independence of a majority of the board to respond. Therefore, when a board refuses a demand, the only issues to be examined are the good faith and reasonableness of its investigation.”<sup>196</sup> Consequently, plaintiffs cannot successfully claim demand futility unless they can show that the decision was so egregious that one can infer bad faith or gross negligence of the board in making the determination about the suit.<sup>197</sup> This contrasts with the other jurisdictions, where an unsuccessful demand does *not* prevent plaintiff shareholders from proceeding with a derivative suit and claims of demand futility are consequently not typically an issue.

In **Israel**, the plaintiff is excused from demand if half or more of the members of the deciding body have a personal interest in the decision, or if there is reasonable concern that demand will prejudice the possibility of obtaining relief.<sup>198</sup> If the corporation decided against bringing a suit or does not bring one within 75 days<sup>199</sup>, the plaintiff may proceed.<sup>200</sup> In admitting the derivative action, the court must be persuaded *prima facie* that the pursuit of the claim would be in the best interests of the company, and that the plaintiff is not acting in bad faith.<sup>201</sup>

The remaining three jurisdictions look primarily at the merits of the claim and whether it is in the best interest of the company: In **Germany**, among other things plaintiff minority shareholders must show facts that justify the suspicion that the corporation suffered injury because of dishonesty or gross violation of the law or the articles of incorporation; and that there are no preponderant reasons relating to the interests of the corporation that tip the balance against the lawsuit.<sup>202</sup> In other words, the courts will look at the severity of the alleged breach of duty, and whether the suit is in the interest of the corporation.<sup>203</sup> After approval of the court the suit has to be filed within 3 months.<sup>204</sup> Under **Singapore’s** law, courts will grant leave to pursue a derivative claim if the complainant is acting in good faith and it must appear “to be *prima facie* in the interests of the company that the action or arbitration be brought, prosecuted, defended or discontinued.”<sup>205</sup> To show the latter, plaintiffs must have a *prima facie* case,<sup>206</sup> moreover, the company must stand to gain substantially (in money or money’s worth) if the action succeeds,<sup>207</sup> and there must be no other remedy available.<sup>208</sup> It has been observed that the Singapore approach risks making the most motivated plaintiffs ineligible to proceed with derivative claims for failure to satisfy the good faith requirement.<sup>209</sup> Likewise, in the **UK**, if plaintiffs cannot establish a *prima facie* case,<sup>210</sup> the court may either dismiss the application or give direction regarding evidence to be provided by the company and adjourn the case.<sup>211</sup> The court must refuse permission either (a) if a person seeking to promote the success of the company would not bring the claim, or (b) the act or omission potentially giving rise to liability has been ratified by the company.<sup>212</sup> Thus, in most cases the majority among shareholder can authorize what would otherwise be a breach of duty. In addition, the court will also assess whether bringing the claim is in the corporation’s best interests. This determination will not only rest on the merits of the claim, but other possible effects of litigation. In addition, among other things, the court is required to take into account whether the plaintiff is acting in good faith, and whether it is likely that the company would authorize the claim if it has not yet been ratified, and whether the company has decided not to pursue the claim.<sup>213</sup> The court can also adjourn proceedings to allow the matter to be ratified.<sup>214</sup>

Note that in the US the court will make its decision based on the plaintiff’s pleadings, i.e. an assertion of facts, regarding a lack of the directors’ disinterestedness. The other four jurisdictions actually will require *prima facie* proof of the plaintiff’s substantive case.

### 2.4.5. Subsequent control over a derivative suit and settlements

In most jurisdictions, the shareholder who initiated the suit (and her lawyer) represents the corporation. For example, in **France**, the corporation must be impleaded into a derivative suit,<sup>215</sup> but this does not create a role for its representatives. In some jurisdictions the law further specifies control over litigation, e.g. in **Italy**, where the shareholders pursuing the action must elect (with a majority) a common representative.<sup>216</sup> In **Singapore**, the court permitting the derivative suit may authorize another person to proceed with it and instruct it accordingly.<sup>217</sup> The one country where the law provides for the possibility of a full takeover of the suit by the corporation is **Germany**. Once a suit has passed the admission stage, the shareholders who successfully brought the application must sue within 3 months on behalf of the corporation.<sup>218</sup> However, the corporation is likewise entitled to pursue the claim, and if it chooses to do so, it steps into the position of the shareholder.<sup>219</sup> It must reimburse the shareholder for litigation expenses.<sup>220</sup>

Once a derivative suit has been admitted, the corporation may still try to take control of the process and in this way undercut minority shareholders' judicial recourse, either by moving for a dismissal of the lawsuit or negotiating a settlement. Generally speaking, common law jurisdictions use courts to control such attempts, whereas civil law jurisdictions tend to involve the shareholder meeting.

In the **United States**, procedural rules provide that derivative suits can be settled, voluntarily dismissed or compromised only with the approval of the court. Shareholders must be notified of a proposed motion to this effect.<sup>221</sup> At that stage, the **Delaware** court will not make their own substantive determinations concerning the merits of the claims, but will only consider "whether the proposed settlement is fair and reasonable in light of the factual support for the alleged claims and defences in the discovery record before it."<sup>222</sup>

One important technique for the corporation to take over litigation in **the United States** is the *special litigation committee*. After a lawsuit has survived the "demand futility" stage discussed in the previous section, it could in principle move into discovery. Since the 1970s, it has become common to establish a "special litigation committee" at this stage, which comprises only directors without an interest in the litigation in order to assess whether the suit is in the best interests of the corporation.<sup>223</sup> An early reaction to this practice was the New York's Court of Appeals' decision in *Auerbach v. Bennett* in 1979, which applied the business judgment rule to the committee's decision provided that it was taken in good faith after sufficient investigation by a committee of disinterested directors.<sup>224</sup> The Delaware courts have taken a less deferential position and developed a two-part test in *Zapata*. Under this precedent, the court "should inquire into the independence and good faith of the committee and the bases supporting its conclusions." Moreover, it "should determine, applying its own independent business judgment whether the motion should be granted."<sup>225</sup> Given the generally deferential attitude of US courts regarding interference with business decisions, some judges have expressed considerable scepticism with respect to this part of the test.<sup>226</sup> The burden of proof is on the committee, i.e. the party applying for a motion to dismiss. The *Zapata* standard also applies in the case of a settlement by the committee. Thus, the court will determine whether it was disinterested, proceeded in good faith and informed by the record, but will also apply its own business judgment regarding the merits of the settlement.<sup>227</sup>

In the other common law jurisdictions, the courts must likewise approve a settlement. While in **Singapore**<sup>228</sup> and **Israel**<sup>229</sup> courts must approve all settlements, in the **UK** "the court may order that the claim may not be discontinued, settled or compromised without the permission of the court" after having granted permission to pursue a derivative claim.<sup>230</sup> In other words, in the UK such an order is in the discretion of the court.<sup>231</sup> Note, however, that in all three jurisdictions the lawsuit is in the hands of the shareholders at this point. Interestingly, the **UK**<sup>232</sup> and **Singapore**<sup>233</sup> law both provide that shareholders may ask for the court's permission to take over a claim that was initially brought by the company (in the UK's case also from other shareholders) but which it is not pursuing diligently. In **Israel** there is even a *derivative defence* analogous to the derivative action, which allows a shareholder to defend a lawsuit



against the corporation on its behalf.<sup>234</sup> In combination, these instruments would seem to make it hard for the company to shut down unwanted derivative litigation without good justification.<sup>235</sup>

**Germany, Italy and Spain** require shareholders votes in the general meeting to renounce or settle a directors' liability claim. All three jurisdictions give minority shareholders exceeding certain thresholds a right to block a settlement. This threshold is 10% of the company's capital in **Germany**,<sup>236</sup> 5% in publicly traded firms and 20% in others in **Italy**,<sup>237</sup> and 3% in publicly traded firms in **Spain** and 5% otherwise.<sup>238</sup> In the **German law of corporate groups**, when a shareholder brings a derivative suit against a controlling entity, non-affiliated shareholders must approve a waiver or settlement in a separate vote, and a minority holding 10% of the company's capital can again veto the decision.<sup>239</sup> Note that these percentages are the same as those to bring derivative suits in private companies in **Italy** and in both private and public companies in **Spain**, thus ensuring that a plaintiff can prevent the corporation from taking the suit out of its hands.<sup>240</sup> In the case of public companies in Italy, however, the threshold to block a settlement are higher than the one to file a derivative lawsuit (respectively, 5% and 2.5%). Some plaintiffs in **Germany**, where the corporation may take over the claim,<sup>241</sup> are not able to block a settlement. However, in Germany a settlement is permissible only three years after the claim arose.<sup>242</sup>

**French** law seems to be the most restrictive with respect to settlements. The corporation cannot limit the shareholders right to sue derivatively,<sup>243</sup> which is why even the shareholder meeting is powerless to stop such litigation. A subsequent suit by the corporation does not lead to a dismissal of a prior derivative action,<sup>244</sup> which can lead to a situation where the corporation is represented both by its legal representatives and its shareholders. A number of procedural debates appear to be unsettled.<sup>245</sup> **Brazilian** law does not explicitly address the control over a derivative lawsuit and its settlement. There is scholarship arguing that the company is not bound by a settlement agreed upon by the shareholder without its consent.<sup>246</sup>

## 2.4.6. Fees and litigation costs

### 2.4.6.1. Distribution of litigation cost in general

The distribution of the risk of having to bear litigation cost is particularly important for derivative litigation. Because shareholders only benefit proportionately from the remedy to the corporation with a gain in the value of their stock, the deterrent effect of high litigation cost can potentially set strong incentives against bringing such a suit.

As a general matter, all jurisdictions in this chapter (besides the US) have some form of a “**loser pays**” system (sometimes called the “English rule” in the US). Under **Brazilian, French, German, Israeli, Italian, Singapore, Spanish and UK** law, the loser must reimburse the winner for the cost of a suit, which typically includes court fees, lawyers' fees and other costs arising under the litigation.<sup>247</sup> An important question is how reimbursable fees are calculated. Sometimes court fees are computed as a fraction of the amount in dispute, which can be very high – and therefore strongly discouraging – for minority shareholder plaintiffs. However, where lawyers' fees are reimbursable, they will typically be repaid only according to the official rate set by law, the government or a bar association, or estimated by the court.<sup>248</sup> Given that law firms with expertise in corporate law often charge much higher rates, this may undercut the effects of the loser pays rule to a certain extent. **Brazilian** law strongly differs from the other jurisdictions in that the winning lawyer is, instead of reimbursement, granted a fee payable by the losing party. This fee is set by the judge and typically corresponds to between 10% and 20% of the award.<sup>249</sup> However, in the derivative action against controlling shareholders the fee is always 20%, without any discretion for the judge.<sup>250</sup>

If there are multiple plaintiffs, they can pool their effort and share costs in most jurisdictions, including when they are liable for reimbursement as losers. In **Germany**, according to scholarly opinion, multiple plaintiffs are responsible in proportion to their shares.<sup>251</sup> In **France**, the civil procedure principle of “*nul ne plaide par procureur*” would normally prohibit one party acting as a representative of another party in civil

procedure. The creation of litigation groups discussed above (Section 2.4.2) is an exception to this principle, as it allows shareholders to make agreements to share litigation costs, including attorney fees and discovery costs.<sup>252</sup>

The single outlier in terms of litigation cost is the **US**, which does not have a “loser pays” system. The Court of Chancery will only use its equitable power to award attorneys’ fees to the successful party in extreme cases, such as when a defendant was found to have engaged in a pattern of bad faith conduct.<sup>253</sup> In practice, one could argue that in shareholder litigation “the starting point is not the American Rule, under which each side bears its own costs, but rather the Delaware Rule, under which the corporation always pays” as a result of a settlement.<sup>254</sup> Consequently, it is extremely rare for plaintiffs having to saddle their own litigation expenses.

In the mid-2010s a debate about fee-shifting bylaws arose in **Delaware**. In a 2014 case, the Delaware Supreme Court permitted a so-called fee-shifting bylaw, which requires the (unsuccessful) plaintiff in a lawsuit against the corporation and its members (including derivative suits) to reimburse the corporation and its members for any costs and expenses incurred in the context of the suit.<sup>255</sup> The Delaware legislature subsequently amended the DGCL to prohibit both fee-shifting bylaws and such provisions in the articles of incorporation concerning “internal corporate claims.”<sup>256</sup> However, so-called “no pay” bylaws that prohibit the firm from reimbursing plaintiffs are still legal, and a number of firms have adopted them.

#### *2.4.6.2 Special rules favouring derivative suits*

In jurisdictions following the “loser pays” principle, the law sometimes modifies it specifically for derivative suits given that minority shareholders have few incentives to bring this kind of claim. Among jurisdictions that have a preliminary procedure (**Germany** for directors’ liability claims, **Israel**, **Singapore**, **UK**), its costs are often the subject of legislation.

Among these, **Germany**, is probably the most plaintiff-friendly jurisdiction. While shareholders petitioning for the admission of a derivative suit still must bear the cost of an application for a derivative suit,<sup>257</sup> the corporation must compensate them not only in the case of success. Shareholders will be indemnified if the reason for the rejection relates to the best interest of the corporation’s interest and the corporation could have, but did not inform the shareholder about it prior to the application.<sup>258</sup> Moreover, if the suit advances past the preliminary stage, shareholders are compensated for their cost even if it is unsuccessful, unless the shareholder supported the application with false information and in doing so acted intentionally or with gross negligence.<sup>259</sup> Plaintiffs are also favoured in the admission procedure in that the amount in dispute is normally capped, thus reducing court fees.<sup>260</sup>

The next jurisdiction in terms of favouring plaintiffs is **Israel**: If a derivative suit is approved by the court, the company must compensate the plaintiff for his fees. It may also order the company to advance him future payments and hold it liable for the defendants’ expenses.<sup>261</sup> However, the fees of the plaintiff’s attorney (in the claim being pursued derivatively) are not freely negotiated, but determined by the court; these fees are paid by the company.<sup>262</sup> If the derivative suit is admitted but ultimately not successful, normally the company must still indemnify the defendant; exceptionally, the court may impose the cost on the individual who initiated the derivative suit.<sup>263</sup>

The **UK** and **Singapore** appear to favour plaintiffs less in this point. In both countries, under the respective statute the court *may* order the company to indemnify plaintiffs for litigation cost (without specifying a connection with the success of the claim).<sup>264</sup> In the **UK**, in a case preceding the current Companies Act and Civil Procedure Rules, the Court of Appeal held that the company should normally be liable for the costs of the claim, even where the litigation is unsuccessful.<sup>265</sup> In practice, the courts seem reluctant to award cost to derivative plaintiffs: Writing in 2016, Andrew Keay reports that shareholders had been awarded cost only in two out of the eight cases where they were successful since the enactment of the Companies Act 2006, and in none of the cases was the award unlimited.<sup>266</sup> Similarly, for **Singapore**

Samantha Tang notes in a recent article that the rarity and uncertainty of such orders makes it unlikely that they will improve incentives for shareholders that are stacked against litigating.<sup>267</sup>

Under legal regime without a preliminary admission procedure for derivative suits, shareholders are typically exposed to normal rules of litigation fees and cost, which are sometimes measured in terms of the full amount in dispute for the corporation overall (not just the plaintiff's percentage). This is true, for example, for the derivative suit against controlling entity under the **German corporate group law**, which means that the fee is measured relative to the full amount of the corporation's claim.<sup>268</sup> This may help to explain why suits of the second type are seldom brought.

In **Italy**, the law stipulates that a minority shareholder plaintiff can be reimbursed not only for litigation cost, but also for the cost of ascertaining the facts.<sup>269</sup> However, scholars point out that the exact amount of reimbursement is up to the court, which cannot take into account the amounts on which plaintiffs have agreed with his "appraisers and advisors." Consequently, a considerable risk of not being fully reimbursed remains.<sup>270</sup> Likewise, in both **Brazil** and **Spain**, normal "loser pays" rules apply to a derivative plaintiff.<sup>271</sup> However, **Spanish** corporate law favour such derivative plaintiffs *ex post* in stating that shareholder plaintiffs *must* be reimbursed by the corporation if they are at least **partially** successful.<sup>272</sup> In other words, a small award suffices to trigger full reimbursement. However, reimbursement is also limited to *necessary* fees.

In addition to all of the foregoing, **Israeli** law also provides that plaintiffs in a publicly traded corporation *may* ask the securities regulator to participate in the expenses when bringing a suit. The decision is made by the Israeli securities regulator, which must be persuaded that the claim is in the public interest and that there is a reasonable chance that the court will approve it as a derivative claim. The court may order the indemnification of the regulator in its final ruling.<sup>273</sup>

#### 2.4.6.3 Advance court fees and security for expenses statutes as financial hurdles

In the comparative corporate law literature, requirements for plaintiffs to advance court fees or to provide security to the corporation for possibly litigation expenses have been discussed extensively as possible hurdles that can discourage derivative litigation. Some authors have suggested that a court decision that reduced the filing fee for derivative suits from a percentage to a modest flat fee resulted in a considerable increase in Japanese derivative litigation in 1993.<sup>274</sup>

In the **United States**, presently nine states allow the corporation to require the plaintiff shareholder to provide it with security for reasonable expenses, including court fees.<sup>275</sup> While this list includes important states such as New York and California, Delaware is a notable absentee. As a matter of historical context, the statutes were recommended in the Wood report of 1944<sup>276</sup> as an instrument of curbing excessive derivative litigation<sup>277</sup> and formerly included in the Model Business Corporations Act.<sup>278</sup> Since the 1980s, the trend has been to repeal such laws.<sup>279</sup>

The statutes differ in various details. Most require the posting of a security only if the shareholder in question holds less than 5% of shares, and several provide exemptions if the market value of shares exceeds a certain threshold (USD 25 000 or USD 50 000). In a number of states, other defendants beside the corporation can also demand security, but in all states, the security includes the other defendants' reasonable costs (should the corporation demand security). In most states, the amount includes attorneys' fees.<sup>280</sup> Typically, plaintiffs can avoid posting a security by asking additional shareholders to intervene in the suit.<sup>281</sup> In addition, many states have general "security for expense statutes" that typically apply only against specific defendants, such as non-residents or foreign corporations.<sup>282</sup>

As a matter of fact, some jurisdictions have requirements of this type that can potentially deter derivative suits, especially if they are measured in terms of the amount in dispute for the entire corporation. For example, in **Germany**, the plaintiff always has to advance part of the court fees in order to pursue a suit.<sup>283</sup> Measured in terms of the amount in dispute, this fee could in principle be excessively high and thus deter derivative litigation,

given that the injury to the corporation will often be in the millions, while a small shareholder will only benefit with a small percentage from compensation. However, for the “lawsuit admission procedure” to enforce director liability, the amount is capped at EUR 500,000 for purposes of calculating court fees, resulting in affordable advance fees of only a few thousand Euros.<sup>284</sup> In jurisdictions that do not have such a pre-trial stage, general rules about court fees could apply and can sometimes be prohibitive.

In **Brazil**, a requirement to advance fees only applies when a minority representing less than 5% of the company’s capital files a derivative suit against a controlling corporation.<sup>285</sup> Plaintiffs must provide security for the legal costs (including court fees and attorney fees) in case of an adverse ruling<sup>286</sup>. Such a guarantee is not required when the plaintiffs against a controlling shareholder represent at least 5% of the stock or when officers and directors are the defendants. CVM recently enacted regulation (Rule 627)<sup>287</sup> decreasing the ownership percentage required to file the lawsuit without offering the security and is evaluating that option in an on-going public consultation.

Table 2.4. Minimum percentages required for plaintiff groups in Brazil

Ownership requirement for calling a shareholders meeting and filing a derivative lawsuit without advancement of fees in listed companies

Outstanding Capital Stock	Percentage
For the first BRL 100 000 000	5%
For the bracket from BRL 100 000 000 to BRL 1 000 000 000	4%
For the bracket from BRL 1 000 000 000 to BRL 5 000 000 000	3%
For the bracket from BRL 5 000 000 000 to BRL 10 000 000 000	2%
For all capital above BRL 10 000 000 000	1%

Source: CVM Rule 627 of 22 June 2020.

By contrast, in **Israel** the law explicitly stipulates that the plaintiff must only pay part of the usual court fee at a rate set by the minister.<sup>288</sup> This means that plaintiffs only need to pay a modest amount when setting the derivative action in motion; once it is approved, the plaintiff shareholders is reimbursed by the company, which will also pay the rest of the fee.<sup>289</sup>

#### 2.4.6.4 Incentivizing lawsuits with contingency and conditional fees

One instrument that is often thought to incentivize lawsuits in representative litigation, especially among shareholders in the US, are attorney’s fees that depend on the outcome of the lawsuit. The **United States** are an outlier here compared to the other jurisdictions because nowhere else are the incentives set by attorney’s fees are such a strong driving force for litigation. In practice, often the main proponent of a lawsuit is specialized law firm that works closely with repeat plaintiffs.<sup>290</sup>

In terms of the legal basis, most derivative suits in the **US** are settled, which is why payments are made from the fund created in the settlement. This “common fund” does not necessarily consist only of financial compensation to the corporation. A settlement may include nonpecuniary components such as changes to the board or management structure. Courts typically apply a “substantial benefits” or “corporate benefits” test in approving settlements.<sup>291</sup> The amount of compensation to the attorney is therefore not only based on the financial pay-out to the firm. In calculating a (contingency) fee, settlements may therefore take other benefits to the corporation into account, such as agreements to change the firm’s governance. This approach has almost uniformly adopted by state and federal courts.<sup>292</sup>

In determining the specific fee, courts either adopt the lodestar method – an hourly fee combined with a multiplier based on the difficulty of the case, or they use a percentage of the award or “substantial benefit” akin to the one used in a contingency fee. Whereas 30% is a relatively common percentage in general<sup>293</sup>,

in one notable Delaware case a rate of 15% was used, arriving at an attorneys' fee of more than USD 300 million out of a judgment of about USD 2 billion.<sup>294</sup> The Delaware Supreme Court justified this award with the enormous economic benefit created by shareholders against defendants who defended the case vigorously using top-notch counsel. Generally, the **Delaware** courts will look at "(i) the amount of time and effort applied to the case by counsel for the plaintiffs; (ii) the relative complexities of the litigation; (iii) the standing and ability of petitioning counsel; (iv) the contingent nature of the litigation; (v) the stage at which the litigation ended; (vi) whether the plaintiff can rightly receive all the credit for the benefit conferred or only a portion thereof; and (vii) the size of the benefit conferred."<sup>295</sup> Thus, when a case settles early, a percentage of around 10-15% may be used, whereas the Court of Chancery will award about 25% if significant procedural steps were taken before a settlement.<sup>296</sup>

Likely the more problematic types of fee awards are those with little tangible economic benefit and yet significant attorneys' fees. These have caused some debate in recent years, given that settlement hearings are non-adversarial, given that plaintiffs, corporations and other defendants all have agreed on the settlement. The court is cast in the role of having to look out for the interests of other shareholders not involved in the litigation.

The single other jurisdictions with few limitations on contingent and conditional fees is **Brazil**, where there is great contractual freedom regarding both types of arrangements. In fact, instead of reimbursement of attorney's fees, Brazilian law provides for a contingent award to the winning plaintiff's attorney using similar criteria as the lodestar method.<sup>297</sup> However the Bar Association limits the total value of owed fees to the total value to be paid to the winning party (i.e., the conditional and fees with other nature received by the lawyer should not be higher than the net award received by the plaintiff).<sup>298</sup>

Other jurisdictions tend to be more cautious in rewarding successful plaintiff lawyers with a contingency fee. Historically, most countries prohibited them, although there has been considerable change in recent years. In **Spain**, the Supreme Court has in recent years established in several cases that the traditional prohibition, which has not been formally repealed<sup>299</sup>, is no longer applicable because it contradicts principles of professional freedom.<sup>300</sup> The **UK** has allowed "damages-based agreements," which are analogous to contingency fees in the US, only since 2013.<sup>301</sup> Reportedly, they have not been used in derivative litigation.<sup>302</sup> In addition, since the Access of Justice Act of 1999, the UK permits **conditional fee** arrangements. Such a fee is defined as "an agreement with a person providing advocacy or litigation services which provides for his fees and expenses, or any part of them, to be payable only in specified circumstances."<sup>303</sup> Such an arrangement may include for a success fee, which "provides for the amount of any fees to which it applies to be increased, in specified circumstances, above the amount which would be payable if it were not payable only in specified circumstances."<sup>304</sup> **France** still prohibits contingency fees ("*pacte de quota litis*").<sup>305</sup> However, French lawyers sometimes arrange in advance for a fixed bonus in case of a success. This bonus, however, cannot be contingent on the damages awarded in the end.<sup>306</sup> Arguably, conditional fee arrangements are far less useful in incentivizing derivative suits than contingency fees because they do not relieve minority plaintiffs of the financial risk, especially under a "loser pays" system.<sup>307</sup>

Otherwise, incentive-oriented arrangements are frowned upon or the exception in many countries. **German** law, for example, permits a contingency fee only to pursue claims for plaintiffs who otherwise would not be able to get judicial recourse, i.e. plaintiffs unable to pay a lawyer.<sup>308</sup> Consequently, such arrangements are not used for shareholder derivative suits. In **Italy**, a fee can be based on the value of a claim or other asset, but lawyers may not be promised a portion of a litigated claim.<sup>309</sup> **Singapore** law prohibits both contingency fees proper and conditional fee arrangements that contemplate "payment only in the event of success in that suit, action or proceeding."<sup>310</sup>

Unconventionally, **Israeli** law states that the court may remunerate the plaintiff who successfully initiated a derivative suit.<sup>311</sup> This is particularly relevant because it might improve incentives for small shareholders to bring such suits given that their benefit is otherwise only the compensation of their reflective loss.<sup>312</sup> **Brazilian** law goes further by establishing an "automatic" reward in the procedure against a controlling corporation under the law of corporate groups: The shareholder who filed the suit is entitled to a premium

– to be made by the controlling shareholder – of 5% of the total amount of the rewarded compensation, besides the reimbursement for the legal expenses. Moreover, the plaintiff's attorney is entitled to fees corresponding to 20% of the total amount of the rewarded compensation.<sup>313</sup>

#### **2.4.7. Assessment and issues for discussion**

Overall, an effective enforcement of derivative claims seems to rest on the presence of a mechanism that gives the initiative and control over litigation to outside shareholders and their attorneys. Such a mechanism relies on at least two factors. First, it is necessary to introduce a screening mechanism (which the **US**, the **UK**, **Germany**, **Singapore** and **Israel** have). Ideally, such a mechanism will weed out abusive lawsuits and permit meritorious ones to go forward. Second, their cost rules need to incentivize suits or at least not set up strong hurdles against them.

Using a demand requirement (as in the **US**, **Germany**, **Singapore** and **Israel**) seems advisable because boards may legitimately decide that a suit is not in the company's best interests. However, the Delaware system where plaintiffs never demand in practice appears not to have the advantages of such a system (the system did not arise by design, but because of the case law). Consequently, it seems preferable to always require demand (barring exceptional circumstances such as the directors' conflict of interest, such as in **Israel**). However, such a system is only likely to work well if it is combined with a specific timeframe within which the board must respond, as it exists in **Israel** and **Singapore**.

A judicial screening mechanism following demand also has the advantage that shareholders' litigation risk can initially be reduced to the cost of the preliminary stage. In fact, systems where shareholders can move directly to a derivative suit appear to be relatively little used. This may be explained by the fact that litigation fees (which plaintiffs will likely have to pay when the suit is unsuccessful) measured on the basis of the alleged harm to the corporation (and not only the plaintiff's reflective injury) creates a strong deterrent. After a suit has passed the pre-screening stage, the law can provide for a different regime for cost. At that point, there is a strong justification for fees being paid by the corporation. **Israel's** solution, where fees are set by the court, are an interesting innovation, as is the securities regulator's ability to fund derivative litigation.

It is a difficult question whether the pre-screening procedure should primarily investigate the directors' ability to make a disinterested decision about whether to sue (as in **Delaware**) or on the substantive merits of a prima facie case brought by shareholders (as in **Germany**, **Israel**, **Singapore**, and the **UK**). One aspect of this policy decision is which types of decision courts are generally better positioned to assess. In the **US**, courts are very hesitant to make substantive business decisions, but the Delaware court is generally well-positioned to assess conflicts of interest. In some countries, judges may be culturally inclined to turn a blind eye to the latter if they are part of the same elite network as managers. By contrast, evident harm to the corporation may be harder to ignore. If we consider a requirement for plaintiffs having to bring a prima facie case, we may also have to consider substantive legal requirements (such as whether a country applies the business judgment rule), which are not the subject of this chapter.

The other standing requirements seem less advantageous or even undesirable. Minimum ownership thresholds only make suits unnecessarily difficult for small shareholders without a corresponding benefit, especially when there is a judicial screening phase that helps eliminate non-meritorious suits.

The contemporaneous ownership requirement also seems questionable, as it is not entirely clear why trading in probabilistic claims should be prohibited. In the **United States** the historical reason for its original introduction was that the federal courts wanted to put an end to the practice of transferring stock in order to create diversity jurisdiction.<sup>314</sup> The requirement thus seems only justifiable where forum shopping is a considerable risk.<sup>315</sup> The "continuous ownership requirement" seems less problematic. It seeks to ensure that the plaintiff's incentives are aligned with those of all shareholders. However, given that the actual driving force behind a suit is usually an attorney who stands to gain from a successful suit or settlement, it is not clear why it should be necessary.

Table 2.5. Derivative suits initiated by shareholders (Part 4)

Country	Brazil	France	Germany	Israel	Italy	Singapore	Spain	UK	USA (Delaware)
Minimum ownership requirement	Between 1% and 5%	None, but 4-7% necessary if suing as a group	1% or EUR 100,000; none in corporate group law	None	2.5% (publicly traded), 20% (other firms)	None	3% (publicly traded), 5% (other firms)	None	None
Ownership before lawsuit	Not required	Not required	Before learning about the alleged breach	Not required	Not required	Not required	Not required	Not required	At the time of the alleged breach
Ownership during derivative litigation	Not required	Not required	Debate about requirement	Debate about requirement	None	None	None	None	Continuous ownership requirement (Rules of Civil Procedure)
Judicial pre-trial screening procedure	No	No	<b>Yes (directors' liability);</b> No (corporate group action)	Yes	No	Yes	No	Yes	Yes
Demand before pre-trial procedure	No	No	Yes (corporation)	Yes (chairman of the board)	N/A	Corporation	N/A	No	Yes in theory; No in practice because of disadvantages for plaintiff
Timeframe for response	N/A	N/A	Reasonable amount of time	45 days	N/A	14 days	N/A	N/A	N/A
Assessment of conflicts of interest of board	N/A	N/A	No	Yes, no demand needed if majority not disinterested	N/A	No	N/A	No	Yes, directors must have lacked disinterestedness either in declining to sue or in decision that gave rise to suit
Assessment of merits in screening procedure	N/A	N/A	Suspicion that of dishonesty or gross violation of the law or the articles; no preponderant reasons against lawsuit	Yes, suit must be in best interests of company	N/A	Yes, suit must be in best interests of company, which includes determination of possible payoffs	N/A	Yes, suit must be in best interests of company	No
Assessment of <b>plaintiff's</b> motives	N/A	N/A	No	Yes, plaintiff must be in good faith	N/A	Yes, plaintiff must be in good faith	N/A	Yes, plaintiff must be in good faith	No
Proof of key issues	N/A	N/A	Plaintiffs must prove facts justifying suspicion	Plaintiff must establish prima facie case	N/A	Plaintiff must establish prima facie case	N/A	Plaintiff must establish prima facie case	Complaint must plead particularized facts
Derivative suit controlled by	Plaintiff shareholder(s)	Plaintiff shareholder(s)	Plaintiff shareholder(s), but corporation may take over suit for <b>directors'</b> liability	Plaintiff shareholder(s)	Plaintiff shareholders or common representative	Plaintiff shareholder(s) or authorized person	Plaintiff shareholder(s)	Plaintiff shareholder(s)	Plaintiff shareholder(s)

Country	Brazil	France	Germany	Israel	Italy	Singapore	Spain	UK	USA (Delaware)
Subsequent abandonment of settlement of suit by corporation	Not possible	Not possible	Shareholder meeting can renounce or settle after 3 years unless 10% minority objects; in corporate group law, non-affiliated shareholders must approve (10% veto)	Court must approve settlement	Shareholder meeting can renounce or settle unless 2.5% minority objects (5% in privately held firms)	Court must approve settlement	Shareholder meeting can renounce or settle unless 3% minority objects (5% in privately held firms)	Court may order that settlement requires <b>court's</b> approval	Court must approve settlement; settlement by special committee requires inquire into disinterestedness of committee and best interests of corporation
Distribution of financial litigation risk	Loser pays (court sets the value of <b>the lawyer's fees</b> as a fraction of the amount in dispute – between 10 and 20%)	Loser pays (official rate)	Loser pays (official rate); court will normally order indemnification of plaintiff for pre-trial procedure for <b>directors'</b> liability claims;	Loser pays, but plaintiff must be indemnified if derivative claim is admitted; subsequent <b>attorney's fees</b> are set by court and paid by company; securities regulator can fund derivative suit	Loser pays (official rate); court may additionally indemnify derivative plaintiffs also for cost of ascertaining facts	Loser pays, but court may order company to indemnify derivative plaintiff for cost of interim procedure at any time	Loser pays, but derivative plaintiffs must be reimbursed if at least partially successful	Loser pays, but court may order company to indemnify plaintiff for permission application	Parties bear their own cost; fee-shifting bylaws not permitted in Delaware
Advance court fees or security for expenses with deterrent effect	Only if against controlling shareholders and below 1-5% of stock	No, only small filing fees	Yes, advance court fees, but capped in preliminary procedure for <b>directors'</b> liability claims	Reduced filing fee that is reimbursed by company if derivative suit is admitted	No	No	No	No	In nine states (including NY, CA) but not Delaware
Contingency fees	Permissible	<b>"Bonus"</b> in the case of success must not depend on amount of award or settlement	Permissible only under circumstance not relevant for derivative suits	N/A because <b>attorney's fees</b> set by court; plaintiff may receive reward	No, fee cannot be based on value of litigated claim	Prohibited	Permissible according to case law	Only conditional fee permitted	Yes. Typically part of settlement, courts apply substantial benefits test

## 2.5. Information asymmetries in representative shareholder litigation

When bringing a derivative lawsuit, outside shareholders generally have a major information disadvantage relative to corporate insiders that are typically the defendants. Compounding the other factors discussed in Section 2.4, this further stacks the deck against litigation initiated by outside investors.

Arguably, shareholder litigation in the **United States** is common in part because US law provides effective mechanisms to address this issue. Once a derivative suit has survived the demand and special litigation stages, it will go into **discovery**. Plaintiffs with a thin basis of evidence may rely on the defendant's obligation to disclose pertinent information.<sup>316</sup> The information gathered may help them to push for a favourable settlement.<sup>317</sup> In Continental European jurisdictions such as **Italy**, for example, fact pleading applies, which means that plaintiffs must specifically indicate from which facts and documents their claims follow; in other words, the plaintiff would have to be able to identify specific documents in advance.<sup>318</sup>



Under this system, plaintiffs are not permitted to go on fishing expeditions to search for documents to substantiate their claims, while “the opponent’s obligations to cooperate are usually strict and quite restrictive.”<sup>319</sup>

Moreover, specifically in derivative suits in **Delaware**, plaintiff shareholders also often use “**books and records**” requests in preparation for a suit.<sup>320</sup> To do so, the prospective plaintiff has to establish a “proper purpose.”<sup>321</sup> The “proper purpose” must be reasonably related to the stockholder’s “interest as a stockholder”, which includes the desire to investigate mismanagement.<sup>322</sup> The standard of proof is quite low: The stockholder must demonstrate, by a preponderance of the evidence, “a credible basis from which the court can infer that mismanagement, waste or wrongdoing may have occurred.”<sup>323</sup> The plaintiff must only present “some evidence” of wrongdoing.<sup>324</sup> In fact, the Delaware courts have encouraged plaintiffs to use “books and records requests” in order to have a better basis for their suits.<sup>325</sup> In other jurisdictions, shareholder inspection rights are not so far-reaching in public companies (where they exist at all). Shareholders are thus largely limited to reviewing financial statements, audit reports or protocols of shareholder meetings that have to be made publicly available.<sup>326</sup>

**Discovery** in the form practiced in the US is not available elsewhere, especially not in civil law jurisdictions. Some jurisdictions provide for a **shift in the burden of proof**. In particular, in **Germany** members of the management or supervisory board have the burden show that they complied with the proper standard of care.<sup>327</sup> This provision likely matters little, given in particular that the German “lawsuit admission procedure” only applies when shareholders can make a prima facie case for gross breaches of duty. Similarly, in **Spain**, the law presumes the directors’ culpability if they violated the law or the articles in causing harm to the corporation.<sup>328</sup>

Discovery is an instrument that goes far beyond derivative suits; any changes in this area would require a fundamental rethinking of procedural law. This chapter therefore does not go into details. It suffices to say that some jurisdictions are making available instruments intended to facilitate information-gathering specifically for derivative litigation. In the **UK**, if the plaintiffs fail to establish a prima facie case for a derivative suit, the court “may give directions as to evidence to be provided by the company.”<sup>329</sup> In **Israel**, a person seeking to file a derivative claim may ask the court – before the filing – that it should instruct the company to disclose documents relating to the process of approving the derivative claim. The court may approve such an application if it is persuaded that the plaintiff has provided preliminary evidence regarding the existence of the conditions for admitting a derivative suit.<sup>330</sup> Reportedly, these rights are relatively limited in practice, which makes information gathering more comparable to a “books and records” request under Delaware law.

Another instrument in some countries is the judicial appointment of a special auditor or investigator upon the request of minority shareholders. Typically, the minority must substantiate serious allegations of wrongdoing or do not receive sufficient responses in the shareholder meeting. In **Germany**, shareholders holding capital stock corresponding to 1% or EUR 100,000 can request an appointment (if the application is rejected by the majority),<sup>331</sup> in **France** 5%,<sup>332</sup> and **Italy** generally 10% and 5% in publicly traded firms.<sup>333</sup> These instruments seem to be used relatively little.

The discussion following this chapter is unlikely to result in the introduction of US-style discovery, which would likely face fierce resistance in many parts of the world because it is considered alien to the legal culture and an abuse litigation practice.<sup>334</sup> However, among the instruments surveyed in this section, the relatively recent legislative innovations in the **UK** and **Israel** seem promising. They are both tied to the preliminary screening procedures in these courts, which means that the court has tight control over which plaintiffs will be given a leg up in order to overcome the severe information problems in collective litigation. This should ensure that discovery procedures are not abused by plaintiffs going on fishing expeditions.

## 2.6. Conclusions

The comparative overview provided in this chapter has shown a variety of approaches in derivative enforcement of corporate claims across jurisdictions. Among other things, jurisdictions differ in the types of claims that shareholders can enforce derivatively, and suitable defendants. Overall, effective enforcement rests on the presence of a mechanism that gives the initiative and control over litigation to outside shareholders and their attorneys. Some jurisdictions require shareholder plaintiffs to first submit the matter before the shareholder meeting, which, however, introduces considerable delays into the process. Screening mechanisms such as minimum share ownership requirements may matter to a certain extent as well.

However, one key issue incentivizing derivative action appears to be whether potential plaintiff shareholders are saddled with financial litigation risk. Systems where shareholders can move directly to a derivative suit appear to be relatively little used.<sup>335</sup> Given that most jurisdictions use some form of the “loser pays rule”, it makes a big difference if there is a preliminary procedure to admit the lawsuit, as it now exists in the **US**, the **UK**, **Germany**, **Singapore** and **Israel**). If it is well-structured, such a mechanism can help in screening for abusive lawsuits and permit meritorious ones to go forward. Such a mechanism can be coupled with a “tiered” system for litigation risk, meaning that plaintiff shareholders initially only risk pay for the cost of the preliminary procedure (or not even that), and that the cost of the follow-up suit is borne by the corporation.

In addition, the existence of an entrepreneurial plaintiff bar incentivized by contingency fees, as well as the availability of a mechanism reducing procedural information asymmetries (such as discovery in the **US**) are important factors. However, introducing these instruments in jurisdictions that are culturally averse to them is politically unlikely and would probably not be a viable goal for a medium-term reform agenda.

Another issue for further discussion is the development of a settlement mechanism. In jurisdictions where derivative litigation is in the hands of the plaintiff shareholders and their attorneys, the latter tend to have the power to settle claims on behalf of the corporation. Settlements are generally desirable because they can save time and expenses. However, in a representative action they also require judicial supervision because of possible conflicts of interest between shareholders as a whole, the representative plaintiff and the attorney.

Finally, a general question for any litigation reform is the efficiency, competence and reliability of the court system. If judges do not have the right kind of training to understand business issues, or if they are overwhelmed with a very large case load, any litigation reform might not yield the expected results because the law in action will differ from the initial expectation. Improving the structure of the judicial system goes beyond this chapter. The question whether the enforcement of shareholder rights can be better served with arbitration is addressed in a companion report.

# Notes

<sup>1</sup> This chapter was commissioned by the OECD as a reference for discussion at the OECD-Brazil workshop on shareholder rights that took place on 22-25 June, 2020. The opinions expressed and arguments employed herein do not necessarily reflect the official views of the OECD or its member countries.

<sup>2</sup> Professor, Fordham University School of Law (mgelter@law.fordham.edu). For research assistance, I thank Rebecca Miller, Ilaria Pizzi, Jeremie Rochard, Jacqueline Schulkin, Natalia Tenaglia, Cecilia Vaino and Artem Volgaev. For valuable comments, I thank participants of the OECD Workshop on June 22, 2020, as well as Renato Beneduzzi, Daniel Blume, Pierre-Henri Conac, Matteo Gatti, Gustavo Gonzalez, Sean Griffith, Aurelio Gurrea-Martínez, Assaf Hamdani, Alan Koh, André Luís Monteiro, Caio de Oliveira, Dan Puchniak, Neshat Safari and Samantha Tang. Caio de Oliveira had primary responsibility for collecting information on Brazilian law. Errors remain my own.

<sup>3</sup> References to data in this chapter were last updated on 14 July, 2020.

<sup>4</sup> **United States (Delaware):** Delaware General Corporations Law (DGCL), most recently amended January 1, 2020, 82 Del. L., c. 219.

<sup>5</sup> **UK:** Companies Act 2006, 2006 ch. 46, as amended by The Risk Transformation Regulations 2017 (S.I. 2017/1212), regs. 1(2), 12(8).

<sup>6</sup> **Singapore:** Singapore Companies Act (Cap. 50, 2006 Ed.), most recently amended by Act 28 of 2019, with effect from 15 January 2020.

<sup>7</sup> **Israel:** Israel Companies Law, No. 5799/1999, Official Gazette No. 1711 of May 27, 1999, p. 189, most recently amended by Amendment No. 33 in section 42 of the Antitrust Law (Amendment No. 21), No. 5729/2019. Israel is sometimes described as a mixed jurisdiction. See, e.g. KONRAD ZWEIGERT & HEIN KÖTZ, AN INTRODUCTION TO COMPARATIVE LAW 235-237 (1998). However, its company law was originally based on a Companies Ordinance of 1929, which was promulgated for the British mandate area of Palestine. Uriel Procaccia, *The New Israeli Company Law: Some Theoretical Highlights*, 2004 EUR. COMP. & FIN. L. REV. 206, 206 n1. Only in 1999 it was superseded by a new code that is discussed here. The law mainly discussed in this report is.

<sup>8</sup> **Brazil:** Lei das Sociedades por Ações (LSA), most recently modified in April, 2019.

<sup>9</sup> **France:** Code de commerce (C. Com.), most recently modified February 14, 2020.

<sup>10</sup> **Germany:** *Aktiengesetz* (Stock Corporation Act) of 6. September 1965 (BGBl. I S. 1089), most recently amended by Artikel 1 of the Law of December 12, 2019 (BGBl. I S. 2637).

<sup>11</sup> **Italy:** Codice civile (C.Civ.) of March 16, 1942, Gazzetta ufficiale No 79 of April 4, 1942, most recently amended June 10, 2019.

<sup>12</sup> **Spain:** Ley de Sociedades de Capital (LSC) of July 2, 2010, most recently amended December 29, 2018.

<sup>13</sup> E.g. Arad Reisberg, *Funding Derivative Actions: A Re-Examination of Costs and Fees as Incentives to Commence Litigation*, 4 J. CORP. L. STUD. 345, 367 (2004).

<sup>14</sup> See e.g. Reinier Kraakman, Hyun Park & Steven Shavell, *When are Shareholder Suits in Shareholder Interests?* 82 GEO. L.J. 1733, 1738 (1994).

<sup>15</sup> See Mark J. Loewenstein, *Shareholder Derivative Litigation and Corporate Governance*, 24 DEL. J. CORP. L. 1, 2, 6 (1999).

<sup>16</sup> Jessica Erickson, *Corporate Misconduct and the Perfect Storm of Shareholder Litigation*, 84 NOTRE DAME L. REV. 75, 86 (2008); see also Loewenstein, *id.*, at 6.

<sup>17</sup> John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 679-680 (1986).

<sup>18</sup> E.g. Martin Gelter, *Why Do Shareholder Derivative Suits Remain Rare in Continental Europe?* 36 BROOK. J. INT'L L. 843, 853 (2012).

<sup>19</sup> Harald Baum & Dan W. Puchniak, *The derivative action: an economic, historical and practice-oriented approach*, in THE DERIVATIVE ACTION IN ASIA 1, 1 (Dan W. Puchniak, Harald Baum & Michael Ewing-Chow eds. 2012).

<sup>20</sup> § 1 of The Israel Companies Law 1999 defines a public company as a company listed on a stock exchange or whose shares have been offered to the public pursuant to a prospectus. Private companies are companies that are not public companies. Thus, there is no distinction by legal form (as there is in the civil law countries). See also Arad Reisberg, *Access to Justice or Justice Not Accessed: Is There a Case for Public Funding of Derivative Claims?* 37 BROOK J. INT'L L. 1021, 1029 (2012) (noting that the "Israeli derivative action is a descendant of the common law derivative action").

<sup>21</sup> Singapore Companies Act s. 18 sets forth criteria under which a company may incorporate as a private company, in particular restrictions on transfer and a limited number of shareholders.

<sup>22</sup> Companies Act s. 4(2)(a) defines a public company as a company whose shares state that it is a public company. The Only public companies may go public, but they are subject to certain additional legal requirements relating in part to capitalization. See s. 755-767.

<sup>23</sup> This scope of the study does not necessarily imply that derivative suits are frequently used in publicly traded firms in all of these jurisdictions. For reasons relating largely to incentives set by litigation costs, they tend to be more common in privately held firms.

<sup>24</sup> The U.S. federal courts also recognize derivative claims brought against corporate directors and officers alleging violations of federal securities laws. Examples include claims alleging that a breach of fiduciary duty by the directors caused the corporation to violate Section 14(a) of the Exchange Act and Rule 14a-9 thereunder when the corporation is alleged to have issued a misleading proxy statement and claims brought under Rule 10b-5 under the Exchange Act, where a controlling stockholder may be alleged to have violated the rule by causing the corporation to repurchase stock at a time at which the price was inflated because of a failure to disclose material adverse information. In addition, Section 16(b) of the Securities Exchange Act of 1934 provides for a statutory right for shareholders to bring suit against an insider to recover short-swing profits on behalf of the corporation.

<sup>25</sup> Delaware uses the *Tooley* test to distinguish between the two types of suits. See *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004). Similarly, in the UK, art. 260(1) of the Companies Act of 2006 defines a derivative claim as "proceedings [...] by a member of a company— (a) in respect of a cause of action vested in the company, and (b) seeking relief on behalf of the company." Courts must not

give shareholders permission to pursue a derivative claim if it could be brought as an individual claim of the shareholder. Companies Act 2006, s. 263(3)(f).

<sup>26</sup> RULES OF THE COURT OF CHANCERY OF THE STATE OF DELAWARE, art. 23.1.

<sup>27</sup> Among other things, this is often thought to be one of the competitive advantages of Delaware incorporation.

<sup>28</sup> On the distinction, see Hans de Wulf, *Direct shareholder suits for damages based on reflective loss*, in FESTSCHRIFT FÜR KLAUS HOPT ZUM 70. GEBURTSTAG 1537, 1538-40 (Stefan Grundmann et al. eds. 2010); Alan K. Koh, *Reconstructing the Reflective Loss Principle*, 16 J. CORP. L. STUD. 373, 373-374 (2016).

<sup>29</sup> Baum & Puchniak, *supra* note 19, at 11.

<sup>30</sup> Baum & Puchniak, *id.*, at 11.

<sup>31</sup> ROBERT CHARLES CLARK, CORPORATE LAW 639 (1986). The Delaware Chancery Court rules describe such a suit as one where “shareholders or members [...] enforce a right of a corporation [...], the corporation or association having failed to enforce a right which may properly be asserted by it.” DEL. CHANCERY COURT RULES, Rule 23.1(a); see also FED. R. CIV. P. 23.1(a), 28 U.S.C.A., FRCP Rule 23.1. See also § 145(b) (describing such claims as any “action or suit in the right of the corporation”).

<sup>32</sup> *Urdan v. WR Capital Partners, LLC*, No. CV 2018-0343-JTL, 2019 WL 3891720, at \*8 (Del. Ch. Aug. 19, 2019).

<sup>33</sup> Arguably, because Delaware corporate law allows firms to opt-out of liability for violations of directors’ duty of care (DGCL § 102(b)(7)), actions for damages are actually harder to bring than requests for injunctions.

<sup>34</sup> s. 216A of the Singapore Companies Act.

<sup>35</sup> Meng Seng Wee & Dan W. Puchniak, *Derivative actions in Singapore: mundanely non-Asian, intriguingly non-American and at the forefront of the Commonwealth*, in DERIVATIVE ACTION IN ASIA, *supra* note 29, at 323, 331.

<sup>36</sup> Dan W. Puchniak & Tan Cheng Han, *Company Law*, 16 SINGAPORE ACAD. L. ANN. REV. 255, 263-264 (2015); Samantha S. Tang, *The Anatomy of Singapore’s Statutory Derivative Action: Why Do Shareholders Sue – Or Not?* J. CORP. L. STUD. 1, 14 (forthcoming 2020).

<sup>37</sup> E.g. Carsten A. Paul, *Derivative Actions under English and German Corporate Law – Shareholder Participation between the Tension Filled Areas of Corporate Governance and Malicious Shareholder Interference*, 2010 EUR. COMP. & FIN. L. REV. 81, 87 (noting that the Companies Act 2006 superseded the common law in the UK).

<sup>38</sup> *Foss v Harbottle*, (1843) 2 Hare 461. See Wee & Puchniak, *supra* note 35, at 331-336 (discussing how the necessity to show “fraud on the minority” made derivative suits hard under the common law).

<sup>39</sup> However, it should be noted that while the common law derivative suit can be used by any company operating in Singapore, the statutory derivative action can only be used by companies incorporated in Singapore. See *Sinwa SS (HK) Co Ltd v Morten Innhau*, [2010] 4 SLR 1.

<sup>40</sup> *Ganesh Paulraj v A&T Offshore Pte Ltd & Anor*, [2019] SGHC 180 (considering an application of a beneficial owner of a first shareholder-plaintiff for leave to pursue a Statutory law derivative action against a second shareholder-defendant); *Ting Sing Ning v. Ting Chek Swee* [2006] SGHC 192 (considering a minority shareholder’s attempts to pursue the common law derivative action against directors-shareholders).

<sup>41</sup> Singapore Companies Act s. 216A(2).

<sup>42</sup> See also Wee & Puchniak, *supra* note 35, at 341 (noting that the statutory mechanism can be used for other purposes besides suing directors).

<sup>43</sup> See Singapore Companies Act s. 216A(2).

<sup>44</sup> Israel Companies Law, §§ 194-206.

<sup>45</sup> Israel Companies Law, § 203. See also ARAD REISBERG, DERIVATIVE ACTIONS AND CORPORATE GOVERNANCE 138 n.70 (2007). Courts have held that there are no formal limits on the types of claims or the defendants. In practice, the burden on a plaintiff targeting “external” parties is much higher, the plaintiff having to demonstrate that the board is so conflicted that it cannot be relied upon to sue third parties. On conflicts see *generally* *infra* notes 198-201 and accompanying text.

<sup>46</sup> Notably, they must be claims of the company (“no reflective loss” principle). Historically, the case *Foss v Harbottle*, (1843) 2 Hare 461, defined the circumstances when shareholders could bring such a claim on behalf of the company.

<sup>47</sup> COMPANIES ACT, s. 260(3), (5)(a) and (b). In privately held firms, members are often directors.

<sup>48</sup> Arad Reisberg, *Shadows of the Past and Back to the Future: Part 11 of the UK Companies Act 2006 (in)action*, 2009 EUR. COMP. & FIN. L. REV. 219, 221

<sup>49</sup> COMPANIES ACT, s. 251(1). Among other things, giving advice in a professional capacity does not qualify someone as a shadow director. s. 251(2)(a).

<sup>50</sup> COMPANIES ACT, s. 251(3).

<sup>51</sup> PAUL L. DAVIES & SARAH WORTHINGTON, GOWER’S PRINCIPLES OF MODERN COMPANY LAW 16-8 (10<sup>th</sup> ed. 2016).

<sup>52</sup> See *Hydrodan (Corby) Ltd (In Liquidation)*, [1994] B.C.C. 161 (finding that approving the disposal of assets by a controlling shareholder does not make the latter a shadow director); BRENDA HANNIGAN, COMPANY LAW 7-29 (4<sup>th</sup> ed. 2016).

<sup>53</sup> See in particular *Iesini v Westrip Holdings Ltd*, [2009] EWHC 2526 (Ch), [2010] BCC 420, 440 (Ch); see also Reisberg, *id.*

<sup>54</sup> The in particular definition in s. 260(1), *supra* note 25.

<sup>55</sup> Moreover, the fact that s. 260(3) includes proposed actions or omissions could be read to mean that plaintiffs could seek injunctive relief against an action that has not yet been taken.

<sup>56</sup> Using s.994 directly, however, is less favorable for a plaintiff shareholder because the company will not have to indemnify the plaintiff minority shareholder. *Iesini v. Westrip Holdings Ltd* [2010], BCC 420, 440 (Ch).

<sup>57</sup> C. com., art. L.225-252.

<sup>58</sup> §§ 147, 148 AktG.

<sup>59</sup> Codice civile, art. 2393-bis.

<sup>60</sup> Ley de Sociedades de Capital, art. 236.

<sup>61</sup> See, respectively, Art. 2393/1 Civil Code and Art. 2407 Italian Civil Code.

<sup>62</sup> Disposizioni per l'attuazione del codice civile e disposizioni transitorie, art 223-septies.

<sup>63</sup> C. Com. art. L.225-251 al. 1.

<sup>64</sup> C. Com. art. L.225-56, II-al. 2.

<sup>65</sup> C. Civ., art. 1843-5 al. 1.

<sup>66</sup> FRANCIS LEFEBVRE, MÉMENTO PRATIQUE FRANCIS LEFEBVRE: SOCIÉTÉS COMMERCIALES ¶¶ 14130, 14131 (2020 ed.). *Infra notes* 158-161 and accompanying text.

<sup>67</sup> C. Com. art. L.225-256 al. 1.

<sup>68</sup> C. Com art. L.225-257.

<sup>69</sup> Cass. com., Oct. 11<sup>th</sup>, 1988, n° 87-10529.

<sup>70</sup> LSA, articles 158(5), 159 and 145.

<sup>71</sup> Cass. com., Mar. 19<sup>th</sup>, 2013, n° 12-14213.

<sup>72</sup> For Germany, see §§ 317, 309 AktG; for Italy, Codice civile, art. 2497; for Brazil, LSA, article 246.

<sup>73</sup> For Italy, see Marco Ventoruzzo, *Experiments in Comparative Corporate Law: The Recent Italian Reform and the Dubious Virtues of a Market for Rules in the Absence of Effective Regulatory Competition*, 2005 EUR. COMP. & FIN. L. REV. 206, 251.

<sup>74</sup> For Brazil, see Julian Fonseca Peña Chediak. *Reflexões sobre a efetividade do regime de responsabilização do acionista controlador*, in LEI DAS S.A. EM SEUS 40 ANOS, 217, 221 (Alberto Venâncio Filho, Carlos Augusto da Silveira Lobo & Luiz Alberto Colonna Rosman eds. 2017); GUILHERME SETOGUTI J. PEREIRA, ENFORCEMENT E TUTELA INDENIZATÓRIA NO DIREITO SOCIETÁRIO E NO MERCADO DE CAPITALIS 75-77 (Quartier Latin 2018).

<sup>75</sup> LSC, art. 236.3.

<sup>76</sup> LSC, art. 236.4.

<sup>77</sup> Cass. crim., Nov. 6<sup>th</sup>, 2019, n° 17-87150.

<sup>78</sup> *Contra* Cass. com., Mar. 21<sup>st</sup>, 1995, n° 93-13721; see also Cass. com., Oct. 6<sup>th</sup>, 1981 n° 77-15264.

<sup>79</sup> Cass. com., QPC Jul. 13<sup>th</sup>, 2016 n° 16-10016

<sup>80</sup> Cass. com., Mar. 29<sup>th</sup>, 2017, n° 16-10016, 2017 REVUE DES SOCIÉTÉS 562.

<sup>81</sup> *E.g.* Cass. com., June 27<sup>th</sup>, 2006, n° 04-15831 (applying the doctrine to a bank that had taken part in decisions of the company through its representatives); see CARSTEN GERNER-BEUERLE & MICHAEL SCHILLIG, *COMPARATIVE COMPANY LAW* 289 (2019) (comparing UK and French law on this issue). See *also* Cass. com., Feb. 14<sup>th</sup>, 2018, n° 15-24146 (discussing a shareholder vote relieving a de facto manager of liability).

<sup>82</sup> See Mariangela Iannoccone & Anna Rosa Adiutori, *The Liability of Directors and the Abuse of Companies*, in *ABUSE OF COMPANIES* 141, 155-156 (Hanne S. Birkmose, Mette Neville & Karsten Engsig Sørensen eds. 2019).

<sup>83</sup> See, *e.g.* explicitly for Germany Sebastian Mock, *Inhalt und Reichweite der Ersatzansprüche in den §§ 147 f. AktG*, 2015 NEUE ZEITSCHRIFT FÜR GESELLSCHAFTSRECHT 1013. In most countries, this follows a rather straightforward interpretation of the language of the law.

<sup>84</sup> See, *e.g.* Martin Gelter, *Mapping types of shareholder lawsuits across jurisdictions*, in *RESEARCH HANDBOOK ON REPRESENTATIVE SHAREHOLDER LITIGATION* 459, 463-466 (SEAN GRIFFITH, JESSICA ERICKSON, DAVID H. WEBBER & VERITY WINSHIP EDS. 2018).

<sup>85</sup> *E.g.* Italy, see Codice civile, art. 2388(4).

<sup>86</sup> DGCL §102(b)(7).

<sup>87</sup> Strictly speaking, Israeli law seems to leave it open what body in the corporation decides about the suit when a prospective plaintiff makes demand. Demand must be made to the chairman of the board (ISRAEL COMPANY LAW § 194(c)), but demand is excused if the corporate body responsible for making the decision is conflicted (ISRAEL COMPANY LAW § 194(d)(1)).

<sup>88</sup> *Ting Sing Ning v. Ting Check Swee* [2006] SGHC 192; [2007] 1 SLR(R) 369.

<sup>89</sup> Companies Act, art. 239(1).

<sup>90</sup> Singapore Companies Act, s. 216B(1).

<sup>91</sup> DEBORAH DEMOTT, *SHAREHOLDER DERIV. ACTIONS L. & PRAC.*, § 5:6 (2019-2020).

<sup>92</sup> These states are Alabama, Arizona, Colorado, Hawaii, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Minnesota, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, Oregon, Pennsylvania, Rhode Island, West Virginia and Wyoming. See DEMOTT, *id.*, § 5.2.

<sup>93</sup> See FED. R. CIV. P. 23.1(b)(3)(a) (plaintiffs must “obtain the desired action from the directors or comparable authority and, if necessary, from shareholders”).

<sup>94</sup> *E.g. Jacobs v. Adams*, 601 F.2d 176, 179 (5th Cir. 1979).

<sup>95</sup> *E.g. Mayer v. Adams*, 141 A.2d 458 (Del 1958).

<sup>96</sup> *E.g. Smith v. Dunlap*, 269 Ala 97, 111 So 2d 1 (1959).

<sup>97</sup> See *Elgin v. Alfa Corp.*, 598 So 2d 807, 817 (Ala 1992) (impractical to make demand on 37,000 policy holders of mutual insurance company); *Grill v. Hoblitzell*, 771 F Supp 709, 712–13 n.5–6 (D Md 1991); *In re Midlantic Corp. S'holder Litig.*, 758 F. Supp. 226, 239 (D.N.J. 1990) (excusing demand because of difficult logistics); DEMOTT, *supra* note 91., § 5.2.

<sup>98</sup> See C. com., art. L.225-253 al. 1.

<sup>99</sup> LSA, article 159.

<sup>100</sup> AktG § 147 I.

<sup>101</sup> Codice civile, art. 2393.

<sup>102</sup> LSC, art. 238.

<sup>103</sup> LSC, art. 239.1.

<sup>104</sup> For Germany AktG § 124 IV.

<sup>105</sup> See AktG § 122 II (stating that only agenda items can be voted on).

<sup>106</sup> *E.g.* Michael Arnold, in 3 MÜNCHENER KOMMENTAR ZUM AKTIENGESETZ, § 147, ¶34 (Wulf Goette & Mathias Habersack eds., 4th ed. 2018); Sebastian Mock, in 1 KOMMENTAR ZUM AKTIENGESETZ § 147, ¶46 (Gerald Spindler & Eberhard Stolz eds., 4th ed. 2019).

<sup>107</sup> LSC, art. 238.1. In addition, **Spanish** law explicitly says that the “[a]pproval of the financial statements shall not preclude action for liability nor constitute a waiver of the action agreed or brought.” LSC, art. 238.4.

<sup>108</sup> LSA, article 159, paragraph 1.



<sup>109</sup> Codice civile, art. 2393(2).

<sup>110</sup> In **Spain**, directors must call a meeting within 2 months. The company's articles may specify a lower threshold. LSC, art. 168. In **Italy**, the threshold is 10% if the company is not publicly traded. Codice civile, art. 2367.

<sup>111</sup> In **Brazil**, pursuant to article 291 of the Brazilian Company Law, the capital markets regulator has the authority to reduce the thresholds for larger companies, based on the outstanding capital stock, and it has effectively done so on 22 June 2020 through CVM Rule 627. See Table 2.5 below for the thresholds defined in this regulation.

<sup>112</sup> LSC, art. 495.2(a).

<sup>113</sup> Testo unico delle disposizioni in materia di intermediazione finanziaria (TUF), art. 126-bis.

<sup>114</sup> For **Germany** AktG § 147 I; for **Italy**, where the decision is taken in an ordinary meeting, Codice civile, art. 2368; for **Spain** LSC, art. 238.1; for **Brazil**, LSA, article 129.

<sup>115</sup> LSC, art. 238.1.

<sup>116</sup> LSA, art. 129, paragraph 1.

<sup>117</sup> Arnold, *supra* note 106, § 147, ¶44.

<sup>118</sup> AktG § 136 I; Codice civile, art. 2373. In **Brazil**, this prohibition originates in an interpretation of the capital markets regulator of the general rule on conflicts of interests (Processo Administrativo Sancionador CVM n. RJ2014/10556).

<sup>119</sup> BGH, Urteil vom 20.01.1986 - II ZR 73/85, NJW 1986, 2051.

<sup>120</sup> Arnold, *supra* note 106, § 147, ¶48; Mock, *supra* note 106, § 147, ¶47; see also OLG München, Urteil vom 28. 11. 2007 - 7 U 4498/07 (noting that the majority shareholder refrained from voting in this case because of the prohibition).

<sup>121</sup> LSC, art. 190.1(e).

<sup>122</sup> Companies Act, art. 239(4).

<sup>123</sup> *E.g.* for Spain LSC, art. 233.1.

<sup>124</sup> AktG § 112.

<sup>125</sup> In Spain: LSC, art. 238.3; in Brazil: LSA, art. 159, Paragraph 2.

<sup>126</sup> Codice civile, art. 2393(5).

<sup>127</sup> In Spain: LSC, art. 239.1; in Brazil: LSA, 159, paragraphs 3 and 4.

<sup>128</sup> AktG § 147 I.

<sup>129</sup> AktG § 147 II, sentence 1.

<sup>130</sup> AktG § 147 II, sentence 2.

<sup>131</sup> Codice di procedura civile, art. 78. See FRANCESCO GALGANO & RICCARDO GENGHINI, 1 IL NUOVO DIRITTO SOCIETARIO 482 (2006); Luca Enriques & Federico M. Mucciarelli, *L'azione sociale di responsabilità da parte delle minoranze*, in 2 IL NUOVO DIRITTO DELLE SOCIETÀ 861, 879 (Pietro Abadessa & Giuseppe B. Portale eds., 2006).

<sup>132</sup> Likely, the main instrument to prevent directors from entering into problematic settlements are their duties of loyalty and diligence.

<sup>133</sup> AktG § 93 IV; Codice civile, art. 2393(6), 2393-bis(1); LSC, art. 238.2, art. 495.2(a).

<sup>134</sup> *E.g.* for Spain Ley de Enjuiciamiento Civil (LEC) 241.1 (each party pays their own costs).

<sup>135</sup> AktG § 147 II, sentence 3. The court must award reasonable fees for cost and time spent to the representative (sentence 4).

<sup>136</sup> Arnold, *supra* note 106, § 147, ¶105.

<sup>137</sup> DGCL § 141(a).

<sup>138</sup> This is by no means a civil law requirement. **France** contrasts with these three countries in that any preconditions and even notice requirements interfering with the exercise of derivative suits are deemed illegal. See C. com., L.225-253, al. 1.

<sup>139</sup> LSC, art. 239.1.

<sup>140</sup> In **Brazil**, there is a separate legal basis for a suit against directors and against a controlling corporation, but the procedure is the same. *Supra* notes 70 and 74 and accompanying text.

<sup>141</sup> This provision in its current shape is of relatively recent vintage and was introduced in 2004. AktG § 148 I, as amended by Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts [UMAG – Business Integrity Act], Sept. 22, 2005, BGBl. I at 2802 (Ger.).

<sup>142</sup> AktG §§ 317, 309 IV.

<sup>143</sup> AktG § 317 I.

<sup>144</sup> See, e.g. DEL. CHANCERY COURT RULES, Rule 23.1(b) (outlying conditions for serving as a representative plaintiff). Somewhat confusingly, the corporation is usually named as party defendant, in spite of the fact that the recovery is to its benefit. *E.g. Dean v. Kellogg*, 294 Mich. 200, 292 N.W. 704 (1940). Courts do not generally allow corporations, which are described as indispensable parties to raise substantive defenses on behalf of the actual defendant, but procedural ones such as lack of jurisdiction over the corporation. *E.g. Levine v. Milton*, 42 Del. Ch. 597, 219 A.2d 145 (1966); *Swenson v. Thibaut*, 39 N.C. App. 77, 250 S.E.2d 279 (1978). On these issues, see FRANKLIN A. GEVURTZ, CORPORATION LAW 413-14 (2<sup>nd</sup> ed. 2010).

<sup>145</sup> FED. R. CIV. P. 23.1(a). See DEMOTT, *supra* note 91, § 4:4.

<sup>146</sup> LSA, art. 159, paragraph 4, and art. 246, paragraph 1. Pursuant to article 291 of the LSA, the capital markets regulator has the authority to reduce the thresholds for larger listed companies, based on the outstanding capital stock of the company, and it has effectively done so in 22 June 2020 through CVM Rule 627. See Table 2.5 below for the thresholds defined in this regulation.

<sup>147</sup> AktG § 148 I.

<sup>148</sup> For Brazil SA, art. 246, paragraph 1, item b; for Germany AktG §§ 317 IV, 309 IV.

<sup>149</sup> LSA, art. 159, paragraph 3. In the analogous situation in **Spain**, the minimum percentage must still be met. See also *supra* note 127 and accompanying text.

<sup>150</sup> Codice civile, art. 2393-bis(1), (2).

<sup>151</sup> LSC, art. 239.1, 168.

<sup>152</sup> LSC, art. 495.2(a).

<sup>153</sup> See Gelter, *supra* note 18, at 856-57.

<sup>154</sup> In the **UK**, the enforcement of directors' liability for unauthorized political expenditure is governed by special provisions. In this case, a suit must be brought by an authorized group of shareholders that normally must hold at least 5% of the company's capital. Companies Act, s. 370(3).

<sup>155</sup> **Singapore** legislators considered introducing a minimum ownership requirement when s. 216A of the Singapore Companies Act was drafted, but decided against it. Tang, *supra* note 36, at 12.

<sup>156</sup> Israel Companies Law, §194(a) (allowing every shareholder or director to bring a suit).

<sup>157</sup> In **Singapore**, the plaintiff does not even have to be a shareholder. Wee & Puchniak, *supra* note 35, at 341, 342.

<sup>158</sup> See C. civ., art. 1984.

<sup>159</sup> C. Com. R.225-169, al. 1.

<sup>160</sup> See C. com., art. R.225-169, al. 2.

<sup>161</sup> C. com., art. L 225-120.

<sup>162</sup> *Hirt v. U.S. Timberlands Serv. Co. LLC*, No. CIV.A. 19575, 2002 WL 1558342, at \*2 (Del. Ch. July 3, 2002). See also DEMOTT, *id.*

<sup>163</sup> *But see* for securities class actions Securities Act § 27(a)(2)(B)(iii); Securities Exchange Act § 21D(a)(2)(B)(iii).

<sup>164</sup> *Hirt v. U.S. Timberlands Serv. Co. LLC*, No. CIV.A. 19575, 2002 WL 1558342, at \*2 (Del. Ch. July 3, 2002). However, when multiple suits proceed separately in different states, there is a risk that dismissal (or other decision) in one suit may result in issue preclusion in other suits. *California State Teachers' Ret. Sys. v. Alvarez*, 179 A.3d 824 (Del.), cert. denied, 139 S. Ct. 177, 202 L. Ed. 2d 38 (2018). The case established three requirements for purposes of preclusion: “ (i) the interest of the nonparty and her representative must be aligned; (ii) “either the party understood herself to be acting in a representative capacity or the original court took care to protect the interests of the nonparty;” and (iii) “sometimes’ notice is required.” 2 MCLAUGHLIN ON CLASS ACTIONS § 9:26 (16th ed.)

<sup>165</sup> This includes only those who acquire shares by operation of the law, e.g. through an inheritance or a merger transaction.

<sup>166</sup> Contemporaneous ownership must be averred in the complaint according to both federal and Delaware rules. FED. R. CIV. P. 23.1(b)(1); DEL. CHANCERY COURT RULES, Rule 23.1(a).

<sup>167</sup> AktG § 148 I 2 no. 1. **Germany** does not require this for suits under the law of corporate groups. Holger Altmepfen *in* 5 MÜNCHENER KOMMENTAR ZUM AKTIENGESETZ, § 317, ¶52 (Wulf Goette & Mathias Habersack eds., 5th ed. 2020)

<sup>168</sup> Companies Act, s. 260(4). The definition of members includes those to whom the shares have devolved by operation of law (e.g. through inheritance or bankruptcy, but who have not yet been formally entered into the register of members). s. 260(5)(c).

<sup>169</sup> DAVIES & WORTHINGTON, *supra* note 51, ¶17-16.

<sup>170</sup> For **Singapore**: Singapore Companies Act, s. 216A(1)(a); For **Israel**: Israel Companies Act, § 194(a). See Arad Reisberg, *Israel: promoting the use of derivative actions*, 24 COMP. LAW. 250, 251 (2003). For **France**: See Cass. com., Jan.26<sup>th</sup>,1970, n° 67-14787. See also MÉMENTO PRATIQUE FRANCIS LEFEBVRE, *supra* note 66, ¶ 14073; for **Spain**: Jesús Quijano, *Comentario al artículo 239*, in COMENTARIO DE LA LEY DE SOCIEDADES DE CAPITAL 1711-1712 (Ángel Rojo & Emilio Beltrán eds.).

<sup>171</sup> Dario Latella, *Shareholder Derivative Suits: A Comparative Analysis and the Implications of the European Shareholders' Rights Directive*, 2009 EUR. COMP. & FIN. L. REV. 307, 319.

<sup>172</sup> WILLIAM T. ALLEN & REINIER KRAAKMAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATIONS 386 (5<sup>th</sup> ed. 2016). See in particular *Lewis v. Anderson*, 477 A.2d 1040, 1046 (Del. 1984) (Delaware Supreme Court case first adopting this requirement). For earlier Chancery cases, see *Harff v. Kerkorian*, 324 A.2d 215, 219 (Del. Ch. 1974), *aff'd in part, rev'd in part*, 347 A.2d 133 (Del. 1975) (“But Delaware law seems clear that stockholder status at the time of the transaction being attacked and throughout the litigation is essential”); *Dell v. Grimm*, No. CIV.A. 5785, 1979 WL 175247, at \*2 (Del. Ch. July 17, 1979). For the proposition that the Delaware Supreme Courts’ adoption of the rule grew out of an imprecise analysis of prior case law, see *Urdan v. WR Capital Partners, LLC*, No. CV 2018-0343-JTL, 2019 WL 3891720, at \*10 (Del. Ch. Aug. 19, 2019).

<sup>173</sup> See UWE HÜFFER & JENS KOCH, AKTIENGESETZ § 148, ¶16 (13<sup>th</sup> ed. 2018) (providing cites to conflicting authorities in the scholarly literature).

<sup>174</sup> In **Israel**, there appears to be at least some academic debate about the possibility. See Reisberg, *supra* note 170, at 251.

<sup>175</sup> C.P.C., art. 111.

<sup>176</sup> Cass. com., Dec 6<sup>th</sup>, 2005, n° 04-10287. Rev. sociétés 2006 p. 570, note A. Cerati-Gauthier, RTD Com. 2006 p.141, note P. Le Cannu. We thank Pierre-Henri Conac for pointing this out.

<sup>177</sup> For the **UK**, Companies Act 2006, s. 261 and 262.

<sup>178</sup> See Paolo Giudici, *Representative Litigation in Italian Capital Markets: Italian Derivative Suits and (if ever) Securities Class Actions*, 2009 EUR. COMP. & FIN. L. REV. 246, 252.

<sup>179</sup> See also Cass. com. Sept. 6<sup>th</sup>, 2016, n° 14-27082 (finding that at this stage the shareholder is not required to prove injury to the corporation).

<sup>180</sup> **Spain** does not require demand on directors, but – as discussed in Section 2.4.1 – normally requires that the question is submitted to the shareholder meeting for a vote unless the allegation involves a violation of the duty of loyalty. Otherwise, minority shareholders can only sue when the directors do not convene the meeting, the company does not bring the suit within a month after an affirmative resolution, or when the meeting decides against liability. See LSC, art. 239.1.

<sup>181</sup> There is some debate whether the demand procedure applicable to directors’ liability suits should apply by analogy. Altmeyden, *supra* note 167, § 317, ¶¶61-66. At least one court of appeals has permitted a minority to request the appointment of a special representative pursuant to the procedure discussed above. OLG Köln, Urt. v. 9.3.2017 – 18 U 19/16. *Supra* notes 129-130 and accompanying text. This suggests that the demand procedure for a suit brought derivatively by a minority shareholder could apply in the corporate group context as well.

<sup>182</sup> DEL. CHANCERY COURT RULES, Rule 23.1(a); see also FED. R. CIV. P. 23.1(b)(3).

<sup>183</sup> Israel Companies Act, § 194(b), (c).

<sup>184</sup> *Infra* notes 192 to 195 and accompanying text.

<sup>185</sup> The court can relieve plaintiffs of this requirement if waiting would cause irreparable harm to the company. REVISED MODEL BUSINESS CORPORATION ACT § 7.42. In theory, in Delaware the board must give its response within a reasonable time once demand has been made. See COX & HAZEN, *supra* note 197, at 440.

<sup>186</sup> Israel Companies Act, § 196.

<sup>187</sup> Israel Companies Act, § 195.

<sup>188</sup> Israel Companies Act, § 196(1). § 1 defines “personal interest” as “a personal interest of a person in an act or transaction of a company, including a personal interest of a relative or another corporation in which such a person or a relative have a personal interest, and excluding a personal interest arising from shareholding in the company; but where the personal interest of a person voting under a power of attorney given to him by another person (even if the former person has no personal interest), and where the vote of a person who has been granted the power to vote on behalf of the person having a personal interest shall be deemed to be a vote of the beneficial owner, regardless of whether the voting discretion is in the voter’s hands or not.” The term relative is defined as “a spouse, sibling, parent, grandparent, descendant, and descendant, sibling, parent of the spouse, or spouse of any of the above.”

<sup>189</sup> Singapore Companies Act, s. 216A(3)(a).

<sup>190</sup> Singapore Companies Act, s. 216A(4). See, Dan W. Puchniak & Tan Cheng Han, *Company Law*, 12 SINGAPORE ACAD. L. ANN. REV. 143, 158-159 (2011); Dan W. Puchniak & Tan Cheng Han, *Company Law*, 14 SINGAPORE ACAD. L. ANN. REV. 179, 187-188 (2013); see also Alan K. Koh, *Excusing Notice under Singapore’s Statutory Derivative Action*, 14(2) AUST. J. ASIAN L. art. no. 3, 7–13 (2013) (proposing guidelines for when notice should be excused and how the court may permit a derivative claim to proceed notwithstanding formal non-compliance with the notice requirement).

<sup>191</sup> AktG § 148 I 1.

<sup>192</sup> *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

<sup>193</sup> *Levine v. Smith*, 591 A.2d 194, 205 (Del. 1991); see also *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) (overruling *Aronson* and *Smith* in that the Supreme Court must make this determination *de novo* on appeal).

<sup>194</sup> GEVURTZ, *supra* note 144, at 428.

<sup>195</sup> *Rales v. Blasband*, 634 A.2d 927, 933 (Del. 1993).

<sup>196</sup> *Spiegel v. Buntrock*, 571 A.2d 767, 777 (Del. 1990).

Note that the disinterestedness of directors is analyzed in the individual case based on the facts pled. Because it is a matter of pleadings, usually plaintiffs will be able to extend their pleadings to the majority of directors even if it first glance only a minority seems to be implicated. GEVURTZ, *supra* note 144, at 426.

<sup>197</sup> See JAMES D. COX & THOMAS LEE HAZEN, *BUSINESS ORGANIZATIONS LAW* 440 (4<sup>th</sup> ed. 2011); ALLEN & KRAAKMAN, *supra* note 172, at 392.

<sup>198</sup> Israel Companies Act, § 194(d)(1), (2). On the definition of personal interest, see *supra* note 188.

<sup>199</sup> The court may permit a sued to proceed before the deadlines if it would make the claim obsolete. Israel Companies Act, § 198(b).

<sup>200</sup> Israel Companies Act, § 197.

<sup>201</sup> Israel Companies Act, § 198(a).

<sup>202</sup> AktG § 148 I 2 and 3.

<sup>203</sup> See, e.g. *Arnold*, *supra* note 106, § 148 ¶46 (noting that the court has full discretion in this decision).

<sup>204</sup> AktG § 148 IV 1.

<sup>205</sup> Singapore Companies Act, s. 216A(3)(b), (c). See also Dan W. Puchniak & Tan Cheng Han, *Company Law*, 17 SINGAPORE ACAD. L. ANN. REV. 235, 244-254 (2016) (summarizing important recent developments in the law surrounding the good faith and interest of the company requirements); Tang, *supra* note 36, at 13-14 (noting that courts have required plaintiffs to show that they are acting in good faith); Alan K. Koh, *Searching for Good Faith in Singapore's Statutory Derivative Action: Much Ado About Something?*, 36 COMP. LAW. 207, 208–09 (2015) (pointing out practical difficulties in application of this requirement).

<sup>206</sup> *Teo Gek Luang v. Ng Ai Tiong*, [1998] SGHC 164; [1998] 2 SLR(R) 426.

<sup>207</sup> *Agus Irawan v. Toh Teck Chye*, [2002] SGHC 49; [2002] 1 SLR(R) 471, para. 8

<sup>208</sup> *Pang Yong Hock v. PKS Contracts Services Pte Ltd*, [2004] SGCA 18; [2004] 3 SLR(R) 1, [22]. On all this, see Wee & Puchniak, *supra* note 35, at 346.

<sup>209</sup> Samantha S. Tang, *Corporate Avengers Need Not Be Angels: Rethinking Good Faith in the Derivative Action*, 16 J. CORP. L. STUD. 471, 490–91 (2016).

<sup>210</sup> Companies Act 2006, s. 261(2)(a).

<sup>211</sup> Companies Act 2006, s. 261(3).

<sup>212</sup> Companies Act 2006, s. 263(2).

<sup>213</sup> Companies Act 2006, s. 263(3).

<sup>214</sup> Companies Act 2006, s. 261(4)(c).

<sup>215</sup> C. com., art. R.225-170, al. 1.

<sup>216</sup> Codice civile, art. 2393-bis(4).

<sup>217</sup> Singapore Companies Act, s. 216(A)(5)(a).

<sup>218</sup> AktG § 148 IV.

<sup>219</sup> AktG § 148 III.

<sup>220</sup> AktG § 148 VI.

<sup>221</sup> DEL. CHANCERY COURT RULES, Rule 23.1(c); FED. R. CIV. P. 23.1(c). The Delaware rule makes an exception when the action has effects only with respect to the specific plaintiff in question.

<sup>222</sup> *Carlton Investments v. TLC Beatrice Int'l Holdings, Inc.*, No. CIV. A. 13950, 1997 WL 305829, at \*1 (Del. Ch. May 30, 1997); see also *Polk v. Good*, *Del. Supr.*, 507 A.2d 531, 536 (1986); also *In re Caremark Derivative Litigation*, Del. Ch., C.A. No. 13670, Allen, C. (Sept. 25, 1996), Mem. Op. at 2.

Whether settlements are advantageous for a litigation mechanism are create additional problems depends in part on the level of scrutiny applied by the courts in practice. This is illustrated by the debate about merger litigation in the **United States**, which is governed by *direct* class action suits (as opposed to derivative suits), but a different form of collective litigation. A vast number of mergers of publicly traded firms were challenged with class actions based on alleged violations of fiduciary duties. Settlements often involved additional disclosures that arguably did not benefit shareholders. They did, however, result in considerable fees being paid to plaintiffs' attorneys. See Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting the Peppercorn Settlement in Merger Litigation: An Empirical Analysis and a Proposal for Reform*, 93 TEX. L. REV. 557, 563-575 (2015). The **Delaware** Court of Chancery opinion of *In re Trulia, Inc. S'holder Litig.*, 129 A.3d 884 (Del. Ch. 2016) stated that settlements would be rejected unless they provided "plainly material" benefits to plaintiffs. See Sean J. Griffith, *Private Ordering Post-Trulia*, in THE CORPORATE CONTRACT IN CHANGING TIMES 292, 297-298 (Steven Davidoff Solomon & Randall Stuart

Thomas eds. 2019) (discussing plaintiff lawyers' reaction to sue in other states more likely to approve settlements).

<sup>223</sup> Minor Myers, *The Decisions of the Corporate Special Litigation Committees: An Empirical Investigation*, 84 IND. L.J. 1309, 1312-13 (2009).

<sup>224</sup> *Auerbach v. Bennett*, 47 N.Y.2d 619, 419 N.Y.S.2d 920, 393 N.E.2d 994 (1979).

<sup>225</sup> *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del 1981).

<sup>226</sup> For example, then Vice Chancellor (and later Delaware Chief Justice) Leo Strine stated that it required him to apply his “oxymoronic judicial ‘business judgment.’” In re Oracle Corp. Derivative Litig., 824 A.2d 917, 928 (Del. Ch. 2003).

<sup>227</sup> *Carlton Investments v. TLC Beatrice Int'l Holdings, Inc.*, No. CIV. A. 13950, 1997 WL 305829, at \*2 (Del. Ch. May 30, 1997).

<sup>228</sup> Singapore Companies Act, s. 216B(2).

<sup>229</sup> Israel Companies Act, § 202 (stipulating that a “request for approval must specify all details of the settlement, including compensation offered to the claimant”).

<sup>230</sup> Civil Procedure Rules, Rule 19.9F.

<sup>231</sup> See Andrew Keay, *Assessing and rethinking the statutory scheme for derivative actions under the Companies Act 2006*, 16 J. CORP. L. STUD. 39, 50-51 (2016) (criticizing the court's discretion).

<sup>232</sup> Companies Act, art. 262, 264 (providing that plaintiffs may ask the court for permission to take over a claim currently litigated by the company or other shareholders that is not being pursued diligently and in a manner that amounts to an abuse of process).

<sup>233</sup> Singapore Companies Act, s. 216A(2).

<sup>234</sup> Israel Companies Act, § 203.

<sup>235</sup> See DAVIES & WORTHINGTON, *supra* note 51, ¶¶17-23.

<sup>236</sup> AktG, § 93 IV.

<sup>237</sup> Codice civile, art. 2393(6), 2393-bis(1). The shareholder meeting also cannot provide an ex ante liability waiver that exculpates future conduct of directors. See Guido Ferrarini, Gian Giacomo Peruzzo & Marta Roberti, *Corporate Boards in Italy*, in CORPORATE BOARDS IN LAW AND PRACTICE 367, 417-418 (Paul Davies, Klaus Hopt, Richard Nowak & Gerard van Solinge eds. 2013).

<sup>238</sup> LSC, art. 238.2, art. 495.2(a).

<sup>239</sup> AktG, §§ 317 IV, 309 III.

<sup>240</sup> See also Giudici, *supra* note 178, at 252.

<sup>241</sup> *Supra* note 219 and accompanying text.

<sup>242</sup> AktG, § 93 IV.

<sup>243</sup> C. com., art. L225-253.

<sup>244</sup> See Cass. com., Sept.27<sup>th</sup>, 2017 n° 15-28835; see also Cass. crim., Dec.16<sup>th</sup>, 2009 n° 08-88305.

<sup>245</sup> See Michel Germain. *Les droit des minoritaires (droit français des sociétés)*, 54 REVUE INTERNATIONALE DE DROIT COMPARÉ 401, 409 (2002).

<sup>246</sup> See CÂNDIDO RANGEL DINAMARCO, *PROCESSO CIVIL EMPRESARIAL* 625, 626, 633 (2010); MARCELO VIEIRA VON ADAMEK, *RESPONSABILIDADE DOS ADMINISTRADORES DE S/A* 492 (2010).

<sup>247</sup> For Germany ZPO § 91; For France C.P.C. (France), art. 696; art. 700; for Italy Cod. proc. civ. (Italy), art. 91, 92; for Singapore see *Tullio Planeta v Maoro Andrea G*, [1994] SGCA 76, [1994] 2 SLR (R) 501; Tang, *supra* note 35, at 22 (noting in particular that costs could be particularly high if the court grants leave to pursue the derivative suit); for Spain, LEC, art. 394.1; for the UK, Civil Procedure Rules, SI 1998/3132, Rule 44.2(2).

<sup>248</sup> In **France**, attorneys' fees are only compensated in all cases according to an official rate. C.P.C. art. 695 no. 7. The court has the discretion to award additional amounts under C.P.C. art. 700, but this still often means that the winning party will not be compensated for a substantial portion of their attorneys' fees. See, e.g., for **Germany**, where the principle of "necessity" applies under ZPO § 91 II, see *Andreas Schulz*, in 1 MÜNCHENER KOMMENTAR ZUR ZIVILPROZESSORDNUNG § 91, ¶ 61 (Wolfgang Krüger & Thomas Rauscher eds., 5th ed. 2016). For **Italy** see *Giudici*, *supra* note 178, at 253. While the law stipulates that the losers must pay the winners' costs of defense, judges will usually refer to the official rates set out in a government decree. Decreto 10 marzo 2014, n. 55, modified by Decreto 8 marzo 2018, n. 37, Decreto 10 Marzo 2014 n. 55. In **Spain**, the losing party is normally only required to indemnify the winning party for attorney's and other professional fees up to a maximum of one third of the amount in dispute (in addition to other fees). The reimbursement may be higher if the losing party acted recklessly. LEC, art. 394.3. In the **UK**, the court has discretion regarding the amount of costs to be reimbursed. Civil Procedure Rules, SI 1998/3132, Rule 44.2(1)(b). In **Israel**, fees are reportedly based on the courts' rough estimate rather than a full account of expenses, which is why courts rarely impose meaning full fees on plaintiffs.

<sup>249</sup> Novo Código de Processo Civil, article 85, paragraph 2. The judge will define the lawyer's fees taking into account his or her dedication, the place where the service was rendered, the nature and relevance of the claim and the services performed by the lawyer as well as the time taken to perform such services.

<sup>250</sup> LSA, article 246, paragraph 2.

<sup>251</sup> Arnold, *supra* note 106, § 148, ¶ 100.

<sup>252</sup> See MÉMENTO PRATIQUE FRANCIS LEFEBVRE, *supra* note 66, ¶ 14077.

<sup>253</sup> *Gatz Properties, LLC v. Auriga Capital Corp.*, 59 A.3d 1206, 1221-22 (Del. 2012) (Chancery Court awarding attorneys' fees to plaintiffs against a fellow member controlling an LLC).

<sup>254</sup> Sean J. Griffith, *Correcting Corporate Benefit: How to Fix Shareholder Litigation by Shifting the Doctrine on Fees*, 56 B.C. L. REV. 1, 30 (2015).

<sup>255</sup> *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554, 556 (Del. 2014). The case concerned a nonstock corporation, but essentially the same would have been true in a regular for-profit corporation.

<sup>256</sup> 2015 DELAWARE LAWS CH. 40 (S.B. 75) (inserting §102(f) and § 109(b) into the DGCL).

<sup>257</sup> AktG § 148 VI 1.

<sup>258</sup> AktG § 148 VI 2.

<sup>259</sup> AktG § 148 VI 5.

<sup>260</sup> GKG § 53(1)5 normally caps the amount in dispute at EUR 500,000, which corresponds to a fee of EUR 3,536 under GKG, Anlage 2.

<sup>261</sup> Israel Companies Act, § 199(B).

<sup>262</sup> Israel Companies Act, § 200a.



<sup>263</sup> Israel Companies Act, § 200. See Reisberg, *supra* note 20, at 1032 (noting that the wording suggests that the success of the case will likely play a role in this decision).

<sup>264</sup> For the **UK**, see Civil Procedure Rules, SI 1998/3132, Rule 19.9E (the court “may order the company [...] to indemnify the claimant against liability for costs incurred in the permission application or in the derivative claim or both”); for **Singapore**, see Singapore Companies Act, s. 216B(3). The court may also order interim measures, see Singapore Companies Act, s. 216A(5)(c).

<sup>265</sup> *Wallersteiner v. Moir (No 2)*, [1975] Q.B. 373 C.A. See DAVIES & WORTHINGTON, *supra* note 51, 17-27.

<sup>266</sup> Keay, *supra* note 231, at 57.

<sup>267</sup> Tang, *supra* note 36, at 22-23 (noting that out of 23 applications only two were granted).

<sup>268</sup> See GKG § 34 (above EUR 500,000, the base fee increases by EUR 180 per EUR 50,000). Moreover, under GKG, Anlage 1, Nr 1210, a multiplier of 3. is applied to the fee. This contrasts with the admission procedure, which has a multiplier of 1.0 according to GKG, Anlage 1, Nr 1640.

<sup>269</sup> Codice civile, art. 2393-bis(5).

<sup>270</sup> Giudici, *supra* note 178, at 254.

<sup>271</sup> For Brazil Novo Código de Processo Civil, arts. 82 and 85; For Spain Blanca Villanueva García-Pomareda, *El Contenido del Acuerdo de la Junta General Sobre el Ejercicio de la Acción Social de Responsabilidad contra los Administradores de las Sociedades de Capital*, 65 CUADERNOS DE DERECHO Y COMERCIO 134 (2016).

<sup>272</sup> LSC, art. 239.2

<sup>273</sup> Israel Companies Act, § 205a.

<sup>274</sup> Mark D. West, *The Pricing of Shareholder Derivative Actions in Japan and the United States*, 88 NW. U. L. REV. 1436, 1463–5 (1994); Mark D. West, *Why Shareholders Sue: The Evidence from Japan*, 30 J. LEGAL STUD. 351, 353 (2001); Kenichi Osugi, *Directors’ Liability and Enforcement Mechanisms in Japan*, in GERMAN AND ASIAN PERSPECTIVES ON COMPANY LAW 47, 53 (Holger Fleischer, Hideki Kanda, Kon Sik Kim & Peter Mülbart eds. 2016); *contra* Dan W. Puchniak & Masafumi Nakahigashi, *Japan’s Love for Derivative Actions: Irrational Behavior and Non-Economic Motives as Rational Explanations for Shareholder Litigation*, 45 VAND. J. TRANSNAT’L L., 1, 48-50, 54-56 (2012).

<sup>275</sup> These states are Alaska, Arkansas, California, Colorado, Nevada, New Jersey, New York, North Dakota, and Pennsylvania. AK Stat § 10.06.435(h); Ark Stat Ann § 4-26-714(c); Cal Corp Code § 800(c), (d); Colo Rev Stat § 7-4-121(3); Nev Rev Stat § 41.520(3), (4); NJ Rev Stat § 14A:3-6(2), (3); NY Bus Corp Law § 627; ND Bus Corp Act § 10-19.1-86(2); PA Bus Corp Law § 1782(c).

<sup>276</sup> F. WOOD, SURVEY AND REPORT REGARDING STOCKHOLDERS’ DERIVATIVE SUITS (1944).

<sup>277</sup> See, e.g. A.F. Conard, *Winnowing Derivative Suits through Attorneys’ Fees*, 47 L. & CONT. PROBS. 268, 284 (1984).

<sup>278</sup> MODEL BUS CORP ACT ANN 2D §§ 49, 3 (1971).

<sup>279</sup> DEMOTT, *supra* note 91, § 3:2.

<sup>280</sup> For a detailed overview see DEMOTT, *id.*

<sup>281</sup> DEMOTT, *id.*, § 3:7.

<sup>282</sup> DEMOTT, *id.*, § 3:3.

- <sup>283</sup> GKG (Gerichtskostengesetz) § 12 I.
- <sup>284</sup> On the amounts, see *infra* Section 2.4.6.
- <sup>285</sup> See *above* Sections 2.2.2 and 2.4.2.
- <sup>286</sup> LSA, article 246, paragraph 1, item b.
- <sup>287</sup> The legal basis is LSA, article 291 and Audiência Pública SDM N° 07/19.
- <sup>288</sup> Israel Companies Act, § 199(a).
- <sup>289</sup> Reisberg, *supra* note 20, at 1031-32.
- <sup>290</sup> See, generally Jessica Erickson, *The New Professional Plaintiffs in Shareholder Litigation*, 65 FLA. L. REV. 1089 (2013).
- <sup>291</sup> *E.g. Saks v. Gamble*, 154 A.2d 767, 770 (Del. Ch. 1958); *Bosch v. Meeker Coop. Light & Power Ass'n*, 101 N.W.2d 423, 426 (Minn. 1960).
- <sup>292</sup> Griffith, *supra* note 254, at 41.
- <sup>293</sup> DEMOTT, *supra* note 91, § 6:18.
- <sup>294</sup> *Americas Mining Corp. v. Theriault*, 51 A.3d 1213, 1261-62 (Del. 2012)
- <sup>295</sup> *In re Emerson Radio S'holder Derivative Litig.*, No. CIV.A. 3392-VCL, 2011 WL 1135006, at \*2 (Del. Ch. Mar. 28, 2011).
- <sup>296</sup> *In re Emerson Radio S'holder Derivative Litig., id.*, at \*3.
- <sup>297</sup> *Supra* notes 249-250 and accompanying text.
- <sup>298</sup> Bar Association Code of Ethics, art. 38.
- <sup>299</sup> Estatuto General de la Abogacía Española (Real Decreto 658/2001, de 22 de junio), art. 44.3.
- <sup>300</sup> Tribunal Supremo, STS 6610/2008 of November 4, 2008; Tribunal Supremo, STS 314/2013 of May 17, 2013.
- <sup>301</sup> Courts and Legal Services Act 1990, c. 41, art. 58AA, as amended by Legal Aid, Sentencing and Punishment of Offenders Act 2012 (c. 10) (amendment coming into force 2013).
- <sup>302</sup> NESHAT SAFARI, RECONSIDERING THE ROLE OF THE DERIVATIVE CLAIM IN THE UNITED KINGDOM 259-260 (Dissertation, City University of London 2018).
- <sup>303</sup> Courts and Legal Services Act 1990 c. 41, art. 58(2)(a), as amended by the Access to Justice Act 1999 c. 22, s. 27.
- <sup>304</sup> Courts and Legal Services Act 1990 c. 41, art. 58(2)(b).
- <sup>305</sup> See, R.I.N. art. 11.3; see *also* Loi n°71-1130 December 31<sup>st</sup>, 1971, art. 10 al. 5.
- <sup>306</sup> See NICOLAS CAYROL, PROCÉDURE CIVILE 800 (2<sup>nd</sup> ed. 2019).
- <sup>307</sup> Reisberg, *supra* note 13, at 380.
- <sup>308</sup> Rechtsanwaltsvergütungsgesetz (Attorneys' Compensation Act), § 4a.
- <sup>309</sup> Legge 31 dicembre 2012, n. 247, Nuova disciplina dell'ordinamento della professione forense, Gazzetta Ufficiale n. 15 del 18 gennaio 2013.

<sup>310</sup> Singapore Legal Profession Act, s. 107(1)(a) and (b) respectively. See also Tang, *supra* note 35, at 21-22.

<sup>311</sup> Israel Companies Act, § 201.

<sup>312</sup> Reisberg, *supra* note 20, at 1034-36.

<sup>313</sup> LSA, article 246, paragraph 2.

<sup>314</sup> Urdan v. WR Capital Partners, LLC, No. CV 2018-0343-JTL, 2019 WL 3891720, at \*9 (Del. Ch. Aug. 19, 2019) (citing Hawes v. Oakland, 104 U.S. 450, 461 (1881)).

<sup>315</sup> On this issue, see in particular J. Travis Laster, Goodbye to the Contemporaneous Ownership Requirement, 33 DEL. J. CORP. L. 673 (2008) (arguing for the abolition of the requirement).

<sup>316</sup> See FED. R. CIV. P. 26; Guido Ferrarini & Paolo Giudici, *Financial Scandals and the Role of Private Enforcement: The Parmalat Case*, in AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US 159, 200-201 (John Armour & Joseph A. McCahery eds. 2006) (explaining that U.S. discovery rules are so far-reaching that they typically shock Continental European lawyers); Frank H. Easterbrook, *Discovery As Abuse*, 69 B.U. L. REV. 635, 636 (1989) (generally discussing the potential abuse in discovery).

<sup>317</sup> See generally Coffee, *supra* note 17, at 701-02 (discussing an explanation for the cost differential between plaintiffs and defendants); see also Érica Gorga & Michael Halberstam, *Litigation Discovery and Corporate Governance: The Missing Story about the “Genius of American Corporate Law”*, 83 EMORY L.J. 1383 (2014).

<sup>318</sup> Giudici, *supra* note 178, at 257.

<sup>319</sup> Rolf Stürner, *Transnational Civil Procedure: Discovery and Sanctions Against Non-Compliance*, 6 UNIF. L. REV. N.S. 871, 876 (2001).

<sup>320</sup> See e.g. *California State Teachers' Ret. Sys. v. Alvarez*, 179 A.3d 824, 831 (Del.), cert. denied, 139 S. Ct. 177, 202 L. Ed. 2d 38 (2018) (citing from a transcript where Chancellor recommended that plaintiffs submit a books and records request).

<sup>321</sup> DGCL § 220(b).

<sup>322</sup> *Seinfeld v. Verizon Commc'ns, Inc.*, 909 A.2d 117, 121 (Del. 2006) (“It is well established that a stockholder's desire to investigate wrongdoing or mismanagement is a ‘proper purpose.’”).

<sup>323</sup> *Id.* at 118.

<sup>324</sup> *Id.* at 123.

<sup>325</sup> Lavin v. W. Corp., No. CV 2017-0547-JRS, 2017 WL 6728702, at \*9 (Del. Ch. Dec. 29, 2017), judgment entered, (Del. Ch. 2018) (“For over twenty years, Delaware courts have encouraged stockholders to use the ‘tools at hand’ (e.g., Section 220) to gather information before filing complaints that will be subject to heightened pleading standards).

<sup>326</sup> See, e.g. for **Singapore** Wee & Puchniak, *supra* note 35, at 345 (“it is usually the case that the complainant, being a mere shareholder, has no access to the company's records, so his or her complaints are often based on the statements of others”).

<sup>327</sup> AktG §§ 93 II 2, 116.

<sup>328</sup> LSC, art. 236.1.

<sup>329</sup> Companies Act, s. 261(3)(a).

<sup>330</sup> Israel Companies Act, § 198a.

<sup>331</sup> AktG, § 141 I.

<sup>332</sup> C. Com. art. L. 225-231.

<sup>333</sup> Codice civile, art. 2409(1).

<sup>334</sup> See, e.g. Vivian Grosswald Curran, *United States Discovery and Foreign Blocking Statutes*, 76 LA. L. REV. 1141, 1142-43 (2016) (discussing French and German laws blocking US discovery).

<sup>335</sup> This finding may not generalize to countries outside the scope of this report. For example, in **Japan** derivative suits are frequently used. See Dan W. Puchniak & Masafumi Nakahigashi, *Japan's Love for Derivative Actions: Irrational Behavior and Non-Economic Motives as Rational Explanations for Shareholder Litigation*, 45 VAND. J. TRANSN'L L., 1, 48-50, 54-56 (2012).

# 3. Report on arbitral proceedings involving collective rights of minority shareholders

---

This chapter presents a comparative study on rules and practices of arbitral proceedings involving collective rights of shareholders in selected jurisdictions, and assesses challenges to the adoption of a class arbitration framework in Brazil. It was co-authored by Andre Luis Monteiro<sup>1</sup> and Renato Beneduzi<sup>2</sup>

---

### 3.1. Introduction

The purpose of this chapter is to present a comparative study on rules of arbitral proceedings involving collective rights of minority shareholders. In other words, the research presented below focuses on private enforcement of shareholders' rights through class arbitration.<sup>3</sup>

Legal systems can provide for private enforcement of shareholders' rights through litigation (i.e., court proceedings) or arbitration. Both in litigation and in arbitration, those rights can be pursued on an individual or collective basis. This chapter specifically addresses class arbitration (arbitration + collective basis). Class arbitration refers to the application of principles of class action suits in the arbitration context and allows for a group of claimants to advance their claims collectively in one action against a single respondent or a group of respondents.

This chapter focuses on procedural rather than substantive issues, i.e., whether or not shareholders or companies have certain substantive rights. In particular, this chapter does not tackle the issue of whether shareholders are allowed to sue the company to seek damages on their personal level (and not on behalf of the company).

Sometimes the chapter mentions specific types of claims (derivative claims, actions challenging general meetings' resolutions, claims seeking damages etc.) in order to address a particular procedural issue in arbitration. However, as this chapter addresses exclusively procedural issues arising from class arbitrations involving corporate claims, we do not compare between countries regarding these specific types of claim. For example, this chapter does not say that derivative claims are available in country A, but not in country B.

It is exclusively focused on the legal basis, which means that political or economic issues are not addressed. In this sense, the sources for the description found below are statutes, rules of arbitral institutions, case law and legal papers.

The information gathered for this chapter served as one of the main references for the workshop that took place on-line on 22-25 June 2020 on the enforcement of shareholder rights in Brazil. The provided material may also serve as an important source for recommendations to be developed by the project team on legislative and regulatory changes.

In addition to the consideration of the case of Brazil, the jurisdictions examined in this chapter are **France, Germany, Italy, Israel, Portugal, Singapore, Spain, the United Kingdom and the United States**. The countries selected reflect an attempt to cover a broad and diverse set of jurisdictions, distinguished by their location (Americas, Asia, Europe and Middle East) and their legal systems (Common Law and Civil Law). These same countries, with the exception of Portugal, are compared in a second chapter prepared for the workshop on derivative suits, to facilitate comparison across both sets of issues.

Some countries required a deep and detailed analysis, as the legal system pertaining to arbitration is abundant and complex (particularly the United States). In certain cases in which countries do not provide class arbitration (Singapore for instance), some limited contextual information is provided that may help the reader understand how shareholder disputes are addressed in such cases (along with additional information available in the previous chapter on derivative suits). The chapter could have opted to exclude such countries, but this would have made the overall comparison of these countries in the workshop across the two chapters more difficult.

Occasionally, even when the country under investigation does not provide class arbitration, this survey makes some brief references to collective actions in judicial settings (i.e. class action). This has been done when their class action proceedings are well designed and can offer useful and suitable solutions to class arbitration (Israel, for example).

The main issues related to the topic examined are (i) the rules dealing with class arbitration, (ii) the allocation of costs between the parties, (iii) the availability of third-party funding, (iv) the confidentiality of the proceedings, (v) the composition of the arbitral tribunal, (vi) the potential participation of the securities and exchange authority as *amicus curiae*<sup>4</sup> in such arbitrations, (vii) the opportunities for shareholders to participate in the arbitrations, and (viii) the effects of the arbitral awards over shareholders (opt-in/opt-out proceedings and *erga omnes* effect of the *res iudicata*<sup>5</sup>).

In terms of structure, this chapter begins by describing the frameworks for arbitration in each of the countries covered. Then, we consider Brazilian Law, briefly explaining the current state of play and pointing out the lessons we can take from other jurisdictions. This part is followed by an analysis of the arbitrability of shareholders' disputes in Brazil, the possibility of agreement on the binding effect of the class arbitration award, the importance of freedom of contract on this matter and, most important, the safeguards we believe must be provided in order to establish a class arbitration procedure in Brazil. Finally, the chapter tackles legal reforms, in particular reforms on institutional rules of arbitration and also on statute law.

The experience and legal frameworks of the nine jurisdictions described in the following sections can provide the basis for a number of useful insights which could help Brazil to improve its own system of enforcement. It is important to highlight that there is no legal system that provides for class arbitration involving shareholders' disputes in publicly-held companies. However, there are legal systems with a sophisticated class action framework, but which cannot be applied to arbitration (e.g. Israel). Some other countries have a well-developed class arbitration system, but which has not been tested in corporate cases (e.g., the US). Some jurisdictions provide useful insights from legal documents of arbitration chambers or supplementary rules (Germany, Spain, US), while in the case of Portugal, draft legislation raises relevant issues for consideration. There are other cases in which arbitration is available for corporate disputes, but only for individual claims, not collective claims (e.g., Spain). There are also those which have arbitration involving corporate disputes, but not for publicly-held companies (e.g., Germany). Last but not least, some jurisdictions simply do not have collective redress (e.g., the UK, except for competition issues, and Singapore).

### 3.2. France<sup>6</sup>

The stipulation of an arbitration clause in a publicly held company's articles of association (*clause compromissoire statutaire*) is admissible under French law but disputes over collective rights of minority shareholders are ordinarily adjudicated only by state courts.

Shareholders who were not parties to arbitral proceedings concerning corporate matters are understood to be bound by the award but they are nevertheless entitled to challenge it before state courts – in the case of domestic arbitration<sup>7</sup> – through the so-called *tierce opposition*<sup>8</sup>.

Moreover, class actions are only a recent innovation first introduced into French law by *Loi n. 2014-344* of 17 March 2014 which does not encompass (as amended) collective disputes between shareholders and the company. Only time will tell whether this recent trend towards (judicial) collective redress will encourage the development of collective arbitration in France<sup>9</sup>.

### 3.3. Germany<sup>10</sup>

Disputes over rights of minority shareholders of publicly held companies (*Aktiengesellschaften – AG*) are not arbitrable under German law<sup>11</sup> and may be adjudicated collectively only by state courts<sup>12</sup>.

Moreover, German case law provides for *erga omnes* effects of arbitral judgments in relation to disputes among shareholders of some types of non-publicly held companies if some specific criteria – about which we will later speak in detail because of their potential usefulness to the development of collective arbitration

in Brazil – are met as per the jurisprudence of the German Federal Court (*Bundesgerichtshof* – BGH)<sup>13</sup>. As disputes among shareholders of publicly held company are not arbitrable, these rules concerning erga omnes effects do not apply to them.

Annex 5 of the *Deutsche Institution für Schiedsgerichtsbarkeit* (DIS) Rules of 2018 sets forth these so-called “supplementary rules for corporate disputes”. With regard to the intervention of third parties in the arbitral proceedings, art. 2.1 of Annex 5 provides that “*in disputes requiring a uniform decision binding all shareholders and the corporation, and in which a party intends to extend the effects of an arbitral award to any shareholder or the corporation who are not named parties to the arbitration (“Concerned Others”)*<sup>14</sup>, the Concerned Others shall be granted the opportunity to join the arbitration pursuant to these DIS-CDR as a party or compulsory intervenor in the sense of Section 69 of the German Code of Civil Procedure (*Intervenor*). This applies, mutatis mutandis, to disputes that can be decided only by a uniform decision binding specific shareholders or the corporation”.

Accordingly, art. 11.1 states that “the effects of an arbitral award extend to those Concerned Others that have been designated as such within the time limits provided in these DIS-CDR, regardless of whether they have availed themselves of the opportunity to join the arbitration as a party or as an Intervenor. The shareholders designated as Concerned Others within the provided time limits agree to recognize the effects of an arbitral award rendered in accordance with these DIS-CDR”.

Annex 5 also provides for the “continuous information of concerned others” (art. 5.1)<sup>15</sup>, “consolidation of jurisdiction in case of parallel proceedings” (art. 9.1)<sup>16</sup>, confidentiality<sup>17</sup> (art. 10) and allocation of costs (art. 12.1)<sup>18</sup>.

### 3.4. Israel

The Israeli Arbitration Law 1968 does not explicitly address the concept and extension of arbitrability. Nevertheless, Section 2(3) establishes that “*an arbitration agreement in a matter which cannot be the subject of an agreement between the parties is invalid*”. This means that any matter that can be written into a contract is arbitrable, which encompasses practically all commercial affairs<sup>19</sup>.

In theory, hence, shareholders’ disputes can be submitted to arbitration<sup>20</sup>. In practice, however, and in spite of the well-developed system of derivative claims and class actions in Israel, arbitration is apparently not the normal way to solve shareholder’s disputes, at least collectively. As some commentators explain, “*the courts have held that in view of the public importance of the class action proceeding it is not appropriate to conduct it by way of arbitration*”<sup>21,22</sup>.

The current Israeli collective redress system is based on the American system<sup>23</sup>. In 2006, the New Class Actions Law came into force and, complemented by the Class Action Regulations 2010, has replaced the entire corpus of sector-specific provisions regarding collective redress<sup>24</sup>. The Class Actions Law applies, among other things, to class actions with relation to securities or units of mutual funds (according to s. 5 of the Second Supplement to the Class Actions Law)<sup>25,26</sup>.

According to s. 11(a), class actions in Israel are opt-out proceedings (default)<sup>27</sup> and the members listed as part of the represented group have to notify the court – within 45 days from the decision that certified the class action or any later date determined by the court – if they do not want to be included in the case. Otherwise, they will be considered as having agreed to be part of the group and will, as a consequence, be bound by any settlement and/or decision. In special circumstances, however, the courts have discretion to determine that a specific class action adopts the opt-in proceedings (exception)<sup>28</sup>.

Settlements depend on court approval, which can be given after the terms of the arrangement have been publicised, and following consideration of any objections filed by the members of the affected group (s. 18(d)). The court will also determine the notification of some authorities (s. 18(c))<sup>29</sup>. According to the



website of the *Israel Securities Authority (ISA)*, the securities and exchange authority normally participates in the process by giving its opinion on the advantages and disadvantages of the proposed arrangement (s. 19(b)(4)). In addition, represented members are allowed to group if they do not agree with the settlement (s. 18(f)). Since the Class Actions Law was enacted, the majority of class actions in the country have been resolved through settlements<sup>30</sup>.

The Act creates an important positive economic incentive in s. 22(a). According to this legal provision, if the court has ruled in favour of the group, it will order the payment of compensation to the leading plaintiff. In other words, this provision enables the court to award compensation to the claimant who commenced the legal proceedings (even in case of settlement). In the context of companies, this works as an important tool to reward shareholders for their activism and for taking risks against the company. The Class Actions Law does not specify the amount of compensation to the leading plaintiff. However, it does elaborate a list of considerations the court should take into account while determining the compensation (s. 22(b)).

The Class Actions Law 2006 also establishes a public fund to finance collective redress. According to s. 27(b), a board was created for the purpose of managing such funds, and it is made up of representatives of consumers, public authorities and regulators. Annually, the government approves a budget for the fund. A separate fund was established to help finance securities class actions and derivative claims. According to Section 55(c) of the Securities Law 1968, the *Israel Securities Authority* is authorised to finance class actions related to the securities and exchange market<sup>31</sup>. The securities and exchange authority “uses its power to finance class actions and derivative actions regularly” and “its main purpose is to reduce the integral asymmetry between the plaintiff and the respondent in these actions”<sup>32</sup>.

Usually, Israeli courts are opposed to private entity third party funding in class actions, however in these cases the courts will seek assurances that the interests of the class members will be conducted in good faith, a criterion that is one of the essential conditions for certification of a class action<sup>33</sup>. According to the OECD’s report on minority shareholders’ protection in the country, Israel has established, at the Tel Aviv District Court and at the Haifa District Court, “Economic Departments” that deal, *inter alia*, with class action and derivative claims, which aims to speed up the resolution of such cases and also enhance the expertise of these courts.

According to s. 24 of the Class Actions Law, a judgment in a class action constitutes a *res iudicata* for all members of the group on whose behalf the class action was conducted, unless otherwise expressly provided for in the law.

In sum, it uses opt-out proceedings and the decision binds all members of the group. As set forth in s. 25 of the Class Actions Law 2006, a long list of acts taken in the course of the class action must be publicised, in particular (i) the court decision that approved the class action, (ii) the request to approve a settlement, (iii) the court decision approving the settlement, and (iv) the court decision on the merits of the class action. Usually, the publication is made in two common daily newspapers<sup>34</sup>.

### 3.5. Italy<sup>35</sup>

Article 12 (3) of the *Legge* n. 366 of 3 October 2001, which reformed Corporate Law in Italy, delegated power to the Government to decide whether to authorise companies’ articles of association to contain arbitration clauses but *Decreto Legislativo* n. 5 of 17 January 2003 expressly excludes publicly held companies from *Legge* n. 366’s scope of application. While this limitation is occasionally criticised by legal scholars it is nevertheless still the law in force in Italy<sup>36</sup>.

Articles 34-36 of *Decreto legislativo* n.5 of 2003 provide for a special and comprehensive regime for corporate arbitration, different in some provisions from the general arbitration regime set forth in the Code of Civil Procedure. Among these special provisions, it is worth mentioning art. 35 par. 2, which allows third parties<sup>37</sup> and other shareholders<sup>38</sup> to intervene in pending arbitral proceedings related to corporate

matters. The intervention of third parties and other shareholders may be indirectly facilitated by the rule under which the request of arbitration needs to be published in the business register (art. 35, par. 1 *Decreto Legislativo* 5 of 2003). In addition, the arbitral tribunal is to be appointed by a person or institution external to the company.

Also of interest to the advancement of collective arbitration in Brazil is art. 816-*quinquies* of the Italian Code of Civil Procedure, which governs how third parties may intervene in pending arbitral proceedings concerning corporate matters<sup>39</sup>. This provision clarifies that the types of intervention referred to by the Code of Civil Procedure in relation to court proceedings (*intervento volontario* and *chiamata in causa*) are equally applicable to arbitral proceedings although only if all parties and the arbitrators agree.

It also remains to be seen whether new rules on *azioni di classe*, which broaden the number of disputes which may be resolved under the class action proceedings, will encourage the development of collective arbitration in Italy. These new rules, which refer to collective rights in general – “*diritti individuali omogenei*” – and not only rights of consumers and users of public services as the old rules did, were expected to enter into force in November, 2020 (as per art. 840-bis of the CPC).

### 3.6. Portugal<sup>40</sup>

The Portuguese Arbitration Act (*Lei n. 63/2011*) does not specifically address arbitration involving shareholders and companies. In spite of such omission, s. 1(1) establishes that “any dispute involving economic interests may be referred by the parties to arbitration, by means of an arbitration agreement, provided that it is not exclusively submitted by a special law to the State courts or to compulsory arbitration”.

The scope of arbitrability is broad enough to allow the submission of shareholders’ disputes to arbitration, although in the absence of a special provision relating to corporate or shareholders arbitrations, unless provided differently in companies statutes, an award rendered in any arbitration dispute between shareholders and the company is only binding to the parties in the arbitration, having no third party effects (which may represent a practical limitation to arbitration involving shareholders and companies)<sup>41</sup>.

Of particular importance for this chapter is (i) a bill regarding corporate arbitration drafted by the *Secretaria de Estado da Justiça* (“Portuguese Ministry of Justice”) in 2018; (ii) a bill regarding corporate arbitration drafted by the *Associação Portuguesa de Arbitragem – APA* (Portuguese Arbitration Association) in 2016<sup>42</sup>; and also (iii) specific arbitration rules to internal company arbitrations drafted again by the *Associação Portuguesa de Arbitragem – APA* (Portuguese Arbitration Association) in 2016<sup>43</sup>.

The bill drafted by the *Secretaria de Estado da Justiça* – as for the provisions mentioned below – is similar to the bill drafted by the *Associação Portuguesa de Arbitragem*. Hence, we have chosen to analyse only the former one.

Bill drafted by the *Secretaria de Estado da Justiça* (“Portuguese Ministry of Justice”) in 2018

According to the proposed legislation drafted in 2018, disputes involving both publicly-held companies and privately-held companies can be submitted to arbitration (s. 1(2)), provided that an arbitration clause has been included in their articles of association (s. 2). According to s. 3(1), all arbitrations and the corresponding final arbitral awards must be electronically registered with the registrar of companies. If the case involves a company with an unknown number of members or more than 20 members, the information related to the arbitrations must be made public on-line (s. 3(2)). All the shareholders who are not formal parties to the arbitration have the right to request the statements and decisions of the case, which will be provided by the company or, in case of default, by the arbitral institution (s. 6). In summary, confidentiality plays a very limited role in corporate arbitrations, at least among the shareholders of the company.

As set forth in s. 4(1), in cases where the claimant is challenging shareholders’ resolutions taken by the general meeting or where the final award is capable of binding third parties (i.e., shareholders who are not

parties to the arbitration), the claimant must list all potentially affected people. In its answer to the request for arbitration, the company must complete or correct such list (s. 4(2)). All the people mentioned by the claimant or the company are allowed to intervene in the arbitral proceedings.

As established in s. 4(4), the arbitral institution will appoint the sole arbitrator or all the members of the arbitral tribunal in arbitrations in which either the subject matter is shareholders' resolutions, or the final award has the power to bind third parties (i.e., shareholders who are not parties to the arbitration).

There is no proposed provision regarding the allocation of costs in corporate arbitrations, which indicates that such arbitrations will be subject to the general rules applicable to all arbitrations.

One of the most important provisions of the bill is described in s. 10(1). Pursuant this provision, the arbitral award will bind all shareholders, regardless of their formal participation or intervention in the arbitration, and regardless of its content (whether it benefits the shareholders or not). Subject to the same conditions, the company is, of course, bound by the decision.

In 2018, the Portuguese Government carried out a public consultation on the draft.

Arbitration rules drafted by the Associação Portuguesa de Arbitragem – APA (Portuguese Arbitration Association)

As mentioned before, APA also drafted specific arbitration rules for corporate arbitrations in 2016. As set forth in s. 5(1), the sole arbitrator or the members of the arbitral tribunal will be appointed by the arbitral institution, unless the parties agree on the name(s) of the arbitrator(s) (s. 5(2)). The system does not allow party-appointed arbitrators. Either the arbitral institution appoints the arbitrator(s), or the parties agree on the name of the sole arbitrator or on the names of the three arbitrators. The well-known system according to which each party appoints one co-arbitrator and then these two co-arbitrators choose the presiding arbitrator is not permitted under the proposed rules.

According to s. 5(3), the arbitral institution will appoint the arbitrator(s) if the relief sought by the claimant is the annulment of shareholders' resolutions or if the arbitral decision is capable of binding people who were not formal parties to the arbitration. In such case, it does not matter if the parties agree or not on the name of the arbitrator(s).

The arbitral institution is not allowed to proceed with the appointment of the arbitrators before the arbitration is registered with the registrar of companies and the company makes the commencement of the case public on its website (s. 5(4)).

In the case of the annulment of shareholders' resolutions or if the arbitral decision is capable of binding people who were not formal parties to the arbitration, s. 6(3) imposes on the claimant the duty to list all potentially affected people, who will be notified of the case. They have the right to intervene in the ongoing arbitration as a co-claimant or as a co-respondent (s. 7(2)).

S. 10 empowers the arbitral institution to determine the consolidation of arbitrations dealing with the same subject matter. In this case, the new arbitral proceeding will be attached to the first ongoing arbitration. The arbitral tribunal in charge of deciding the consolidated case is the one appointed in the first arbitration. However, if the subject matter of the new arbitration is an action for annulment of a shareholders' resolution, the arbitral institution is authorised to dismiss the case straight away (s. 11). It makes sense as the decision taken by the arbitrators of the first arbitration will bind all the shareholders and the company.

Notwithstanding the fact that the proposed bill and rules of arbitration are not in force, they serve as a helpful guide for those who want to draft similar provisions in their companies' articles of association.

### 3.7. Singapore<sup>44</sup>

Shareholders' disputes in Singapore are, in general, arbitrable. Neither the Arbitration Act nor the International Arbitration Act prohibits shareholders from submitting to arbitration their conflicts against other shareholders and/or the company. In its turn, the Companies Act expressly mentions the word arbitration in s. 216A, 306, 366 and also in the Eleventh Schedule.

According to s. 216A(2), which regulates derivative claims, “*subject to subsection (3), a complainant may apply to the Court for leave to bring an action or arbitration in the name and on behalf of the company or intervene in an action or arbitration to which the company is a party for the purpose of prosecuting, defending or discontinuing the action or arbitration on behalf of the company*”. Case law supports the arbitrability of internal company conflicts. The authority on this subject matter is the *Tomolugen v. Silica* case, decided by the Singaporean Court of Appeal in 2015<sup>45,46</sup>.

In terms of collective redress, however, Singaporean Law is quite restrictive. The system is mostly based on English Law and, therefore, does not provide a collective mechanism like that seen in US-style class actions<sup>47</sup>. Unlike English Law, there is no Group Litigation Order (GLO) in Singapore. The only tool in Singapore to deal with multiparty claims is the representative action, under order 15, rule 12 of the Rules of Court<sup>48</sup> (which mirrors the representative action procedure in English Law under Part 19.6 of the Civil Procedural Rules<sup>49</sup>).

According to this rule, two or more members of a group can bring or defend a claim on behalf of themselves and other members provided they share what is called “the same interest”. The Singaporean Court of Appeal has been interpreting this concept in a “broad and flexible manner”, requiring only “one or more significant issues of fact or law common to all the claimants for determination by the court”<sup>50</sup>.

Representative actions differ greatly from US-style class actions because all represented members must be identified and agreed before litigation commences<sup>51</sup>. The decision, against or in favour of the group, binds all represented members (O. 15, r. 12(3))<sup>52</sup>.

There is no express prohibition against using representative action in a company context. In fact, representative action can be used in all areas of law. However, commentators report that only two representative actions were brought before the Singaporean courts between 2000 and 2019<sup>53</sup>. The *Raffles Town Club* case is a good example, in which about 5,000 members sued the club's managers for misrepresentation and breach of contract<sup>54</sup>.

### 3.8. Spain<sup>55</sup>

Article 11-*bis* of the Spanish Arbitration Act (as amended in 2011 and 2015) allows publicly held companies<sup>56</sup> to include arbitration clauses in their articles of association (so-called *arbitraje estatutario*)<sup>57</sup>.

In this context, arbitral institutions are encouraged to go further and to create special rules to regulate corporate arbitration. This chapter has chosen to mention the special rules of three very important Spanish arbitral institutions: *Corte de Arbitraje de Madrid (CAM)*, *Corte Civil y Mercantil de Arbitraje (CIMA)*, and the recently launched *Centro de Arbitraje Internacional de Madrid (CIAM)*.

As for arbitrators, s. 52(3) of the rules of arbitration of the *Corte de Arbitraje de Madrid* (“Court”) establishes that “the appointment of the sole arbitrator or, where appropriate, of the three arbitrators forming the arbitral tribunal, will be decided by the Court, unless after the dispute arises all parties freely agree on a different system to appoint the arbitrators, so long as the principle of equal treatment to the parties is respected”.

As a rule, the arbitrators are appointed by the Court, not by the parties. Exceptionally, parties are allowed to appoint the arbitrators if they agree on the appointing process after the dispute emerges. Similar

provisions can be found in s. 4(3) of the rules of the *Corte Civil y Mercantil de Arbitraje (CIMA)* and s. 68(3) of the rules of the *Centro de Arbitraje Internacional de Madrid (CIAM)*.

S. 52(5) of the rules of arbitration of the *Corte de Arbitraje de Madrid* allows third parties to join the arbitration, as co-claimants or co-respondents, before or after the appointment of the arbitrators. As established in the last part of such provision, “the third party requesting its inclusion in the arbitration shall adhere to the procedure at its current stage”. This means, for example, that the third party who joins the arbitral proceedings after the appointment of the arbitrators must accept the composition of the arbitral tribunal. The rules of arbitration of the *Centro de Arbitraje Internacional de Madrid (CIAM)* contain the same provision (s. 68(5)).

According to s. 52(6) of the rules of arbitration of the *Corte de Arbitraje de Madrid*, the Court has the power to consolidate two or more pending arbitrations related to the same company. According to the first part of that provision, “if a party files a request for arbitration in relation to a company conflict for which there is already an ongoing pending arbitration proceedings, the Court may, at the request of either party and after consulting with all of them, decide to join the request for arbitration to the oldest ongoing proceedings after hearing all the parties”. The rules of the *Corte Civil y Mercantil de Arbitraje (CIMA – s. 4(5))* and the rules of the *Centro de Arbitraje Internacional de Madrid (CIAM – s. 68(6))* adopt the same approach.

In the case of the *Corte de Arbitraje de Madrid*, the rules go further and also establish that after the appointment of the arbitral tribunal of the first arbitration, consolidation will only be acceptable if all the parties involved agree to the request for joinder (s. 52(6), final part). The arbitral tribunal in charge of deciding the first case will decide the consolidated cases.

As a rule, arbitral proceedings are confidential under Spanish law, which is followed by the three arbitral institutions. However, the rules of arbitration of the *Corte Civil y Mercantil de Arbitraje* diverge from the general rule with regard to corporate arbitration. S. 63(1) provides that “the Court will publish on its website the awards resolving corporate conflicts which are registrable, maintaining the names of the Arbitrators, but deleting all references to the names of the parties and data which might readily identify them, and provided that neither party has objected expressly to the publication within a period of thirty (30) days from the date on which the award was rendered”. However, the website of the CIMA (as of February 2020) shows no sign that this provision is being enforced.

The Spanish Arbitration Act (s. 37.6) remains silent on the terms of how the costs shall be distributed among the disputing parties, but legal scholars understand that the general rule is “costs follow the event”<sup>58</sup>. The rules of the arbitral institutions adopt the “costs follow the event” approach (unless the parties agree otherwise), mirroring the rules found in the Spanish Civil Procedure Code. Accordingly, s. 40(6) of the rules of the *Corte de Arbitraje de Madrid* establishes that “unless the parties agree otherwise in writing, the arbitrators may justify their orders on arbitration costs on the basis of the principle of costs follow merits, unless the arbitrators consider that in the particular circumstances of the case the application of this general principle is inappropriate”. The same approach can be found in s. 45(7) of the rules of the *Centro de Arbitraje Internacional de Madrid (CIAM)*.

The rules of the *Corte Civil y Mercantil de Arbitraje (CIMA)* also make clear that costs are allocated among the parties by the arbitrators at the end of the proceedings on the basis of what the parties agreed upon. But in default of agreement costs normally follow the event in proportion to the degree of success<sup>59</sup>.

Third party funding is becoming increasingly popular in Spain<sup>60</sup>, under the guise of a silent partnership according to the prevailing opinion among Spanish scholars<sup>61</sup>. According to commentators, “Spanish law neither expressly permits nor prohibits third-party litigation funding” as well as “in Spain there are no specific legislative or regulatory provisions applicable to third-party litigation funding”<sup>62</sup>. Nevertheless, third-party funding is permitted in Spanish Law provided “third-party funding agreements do not violate the law, morality or the public order of Spain”<sup>63</sup>.

In practice, they are considered lawful as atypical forms of contract as per s. 1255 of the Spanish Civil Code. It is also said that “Spanish law does not contemplate limits on the fees and interest funders can charge” as well as “Spanish public bodies have not expressed a particular interest in or oversight over third-party litigation funding”<sup>64</sup>. It is worth highlighting that s. 5.2.i) and 23 of the rules of arbitration of the *Centro de Arbitraje Internacional de Madrid (CIAM)* expressly contemplate third-party funding, which is strong proof that such a financial mechanism is accepted under Spanish arbitration law.

The intervention of third parties or market regulators in pending arbitral proceedings as *amicus curiae* are not expressly regulated by Spanish law. But s. 9(2) of the rules of arbitration of the *Corte de Arbitraje de Madrid* states that “the arbitrators may, at the request of any party and after hearing all of them, allow the appearance of one or more third parties as parties to the arbitration”. S. 13 of the CIMA Rules provides that “*at the request of any party and after assessment of the relevant circumstances, the Court may allow the intervention of one or more third parties as additional parties to an arbitration procedure, provided that the requesting party makes this application in its first submission to the Court – in accordance with the Rules – and proves that the third party or parties invited to join are parties to the arbitration agreement on which the dispute is based*”. The fact that third parties may not intervene if not invited by one of the parties to the proceedings limits substantially the scope of application of these provisions.

Finally, “the arbitral award shall be binding on all shareholders, regardless of whether they have taken part in the arbitration or not”<sup>65</sup>.

### 3.9. United Kingdom

The review of the United Kingdom has focused in particular on laws applicable to England and Wales. English Law does not prohibit shareholders’ disputes (including derivative claims) from being submitted to arbitration, although shareholders’ disputes in England and Wales are in practice nearly always handled through non-adjudicatory methods or before the courts. In fact, there is no legal provision in the Companies Act 2006, nor in the Arbitration Act 1996, which prevents shareholders from using arbitration to solve conflicts<sup>66</sup>.

This conclusion is supported by *Fulham v Richards*<sup>67</sup>, decided by the Court of Appeal in 2011. The Court determined that shareholders’ disputes are arbitrable, although in cases involving unfair prejudice, some forms of relief can only be granted by courts, as for example winding-up orders, orders for the regulation of the company’s affairs, or orders for restraints upon the company’s power to make alterations in its articles<sup>68</sup>. Therefore, where such relief have been sought by the claimant, arbitration is not the most suitable method for solving disputes<sup>69</sup>. The reason behind this conclusion is that orders of such kind would inevitably impact third parties (other shareholders, creditors etc.) who are not part of the arbitral proceedings.

In shareholders’ disputes, the general rule in England and Wales is that a member of a company cannot claim redress on behalf of the company, since the company is a separate legal person. This doctrine is called the *proper claimant principle*<sup>70</sup>. However, as an exception to this general rule, English Law allows derivative claims in Part 11 (s. 260-264) of the Companies Act 2006 as well as in Part 19 (s. 19.9 and Practice Direction 19C) of the Civil Procedure Rules. In England and Wales, derivative claims are designed for situations where a company is alleged to be entitled to claim a remedy but declines to pursue it<sup>71</sup>. Whether successful or not, the outcome of the derivative claim binds the company and prevents other shareholders from repeating the same claim in future legal proceedings<sup>72</sup>.

As we can see, English Law does permit arbitration of shareholders’ disputes (including derivative claims), but for some cases arbitration is not the most suitable method of dispute resolution, as the arbitrator enjoys less extensive powers than the courts<sup>73</sup>. This is one of the reasons why arbitration of internal company disputes, and, in particular, shareholders’ grievances, is uncommon in English Law<sup>74</sup>. Other reasons are

the high costs incurred by the claimant (without any sort of premium to the shareholder who brings the claim), and the effectiveness of non-adjudicatory initiatives at the disposal of the shareholders, such as the use of media pressure in some cases<sup>75</sup>.

Regarding class actions, legal scholars unanimously say that English Law does not prescribe legal proceedings like US-style class actions<sup>76</sup>.

The only exception is set forth in s. 47B of the Competition Act 1998 (as amended by schedule 8, paragraph 5 of the Consumer Rights Act 2015), which came into force in 2015. The legal provision enables consumers and businesses to bring class actions for losses suffered as a result of an infringement of Competition Law before the Competition Appeal Tribunal (CAT). They are on an opt-out basis and the claimant does not need to identify all members of the represented class. There are some important differences between the English class action based on violation of competition law and US-style class actions, in particular (i) the regime of allocation of costs (= costs follow the event), (ii) the stricter certification process and (iii) the prohibition of use of damage-based agreements<sup>77</sup>. Besides that, the scope of applicability of such class actions is much narrower than the American class action.

Apart from the class actions based on violations of Competition Law, English Law also provides for the so-called Group Litigation Orders (GLO). GLO are not a specific type of action, but rather a case management tool at the disposal of the courts. It only takes place when the court issues a GLO either by granting a party's application, or by its own motion<sup>78</sup>. Curiously, there is no threshold criteria and certification process set forth in the Civil Procedure Rules; instead, it is at the discretion of the judge. GLO is opt-in only<sup>79</sup> and the decision taken through this legal tool only binds those who have opted to participate in the collective redress.

Legal scholars agree that GLO is not suitable for arbitration<sup>80</sup> since, under the Arbitration Act 1996, arbitrators are not allowed to order consolidation of different claims unless all parties to the arbitration agreement agree<sup>81</sup>. Furthermore, English Law implies the confidentiality of the arbitral proceedings, which creates an impassable obstacle to class arbitration, in which publicity is crucial<sup>82</sup>. These legal features make it practically impossible to address a collective or mass claim through arbitration in England and Wales without significant legislative change<sup>83</sup>.

### 3.10. United States<sup>84</sup>

The US legal system is well-known for its collective redress procedures (class actions and mass actions). Governed by Rule 23 of the Federal Rules of Civil Procedure (federal courts)<sup>85</sup>, class actions represent a sophisticated legal tool at the disposal of claimants who are united by common questions of law or fact and provide a mechanism for claimants to collectively pursue claims that would otherwise be too small (*small-dollar claims*) to justify the expenses of an individual litigation. The mechanism facilitates access to justice and promotes efficiency in the judicial system although it could arguably be said that they have become a form of “lawyer-driven litigation” used to pressure defendants into settling claims, even very weak claims, so as to avoid the costs and potentially massive liability<sup>86</sup>.

Class actions can be used in a wide range of legal matters in the US, including consumer claims, securities claims, antitrust claims, mass tort, product liability claims, and civil rights. In terms of available relief, the claimant is allowed to seek damages (including punitive damages), restitution, or injunctive or declaratory relief<sup>87</sup>. It is estimated that more than 10,000 new class actions are filed each year in the United States<sup>88</sup>. In the judicial context, the American system features class actions with three essential characteristics: (i) the class certification phase, (ii) opt-out proceedings and (iii) binding decisions on all class members (irrespective of the result, whether or not favourable to them, except those who have decided to opt-out previously)<sup>89</sup>.

Class arbitrations<sup>90</sup> date back more than 30 years in the US<sup>91</sup>, but the boom started in 2003 after the case *Green Tree v Bazzle*<sup>92</sup>, where the Supreme Court held that arbitration clauses that make no mention (i.e. silent clauses) of collective redress do not preclude class arbitrations. *Green Tree v Bazzle* had four main consequences. Firstly, the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS) issued specific rules regulating class arbitrations (which are briefly described below)<sup>93</sup>. Secondly, the number of class arbitrations multiplied, most of them based on arbitration clauses that were silent in regard to collective redress<sup>94</sup>. Thirdly, the business sector started including clauses in their contracts containing class arbitration waivers, which would prevent consumers from commencing class arbitration (or being part of a represented group)<sup>95</sup>. The fourth consequence was the discussion about the validity of these waiver clauses<sup>96</sup>.

The issue has been frequently revisited by the Supreme Court in cases such as *Stolt-Nielsen v. AnimalFeeds*<sup>97</sup>, where the Supreme Court found that the arbitrators had exceeded their authority since the parties had expressly agreed that the arbitration clause did not allow class arbitration<sup>98</sup>, *AT&T v. Concepcion*<sup>99</sup>, where it decided that courts must place arbitration agreements on an equal footing with other contracts and, therefore, enforce them according to their terms<sup>100</sup>, and *American Express Co. v. Italian Colors Restaurant*<sup>101</sup>, where it understood that “*arbitration is a matter of contract*” which means that courts must “*rigorously enforce arbitration agreements according to their terms*” unless the FAA has been “*overridden by a contrary congressional command*”.

Finally, in 2019 the Supreme Court decided the case *Lamps v. Varela*<sup>102</sup>. The case involved the disclosure of employees’ tax information by another employee who had been tricked by a hacker. In deciding the case, the Court reaffirmed its holding according to which “*an ambiguous agreement cannot provide the necessary contractual basis for concluding that the parties agreed to submit to class arbitration*”. The Court reiterated that arbitration is strictly a matter of consent and that courts may not infer consent to participate in class arbitration without an affirmative contractual basis for concluding that the party had agreed to do so. In a plurality decision, the Court concluded again that “*silence is not enough and ambiguity does not provide a sufficient basis to infer consent*” to arbitrate disputes collectively.

The review of the US Supreme Court case law concerning class arbitration allows us to draw seven important conclusions: (i) class arbitrations are not theoretically incompatible with the Federal Arbitration Act<sup>103</sup>, (ii) the availability of class arbitrations is a matter of contract<sup>104</sup> (and express consent), (iii) silent arbitration clauses do not furnish contractual basis to compel one of the parties to arbitrate on a collective basis<sup>105</sup>, (iv) class arbitration clauses are enforceable provided that they are expressly agreed by the parties<sup>106</sup>, (v) clear and unmistakable class arbitration waiver clauses are also enforceable<sup>107</sup>, (vi) for now, the question of whether an arbitration agreement allows for class arbitration should be left for arbitrators to decide, subject to minimal and deferential judicial review<sup>108</sup>, and (vii) the careful drafting of arbitration clauses concerning class arbitration is of paramount importance<sup>109</sup>. This outcome provoked strong reactions – in particular because of the admissibility of the waiver clause – in consumer groups and regulators, which have been trying to implement some changes in the law<sup>110</sup>.

Rules concerning class arbitration are expressly provided for by the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS). The AAA Supplementary Rules for Class Arbitrations, for example, apply when “*a party submits a dispute to arbitration on behalf of or against a class or purported class*”<sup>111</sup>. The rules do not specify a minimum number of people in the represented group, which is left to the discretion of the arbitral tribunal. Regarding the arbitrator appointment process, s. 2 states that “*at least one of the arbitrators shall be appointed from the AAA’s national roster of class arbitration arbitrators*”. Two pieces of information are noteworthy: (i) the arbitral institution has a specific list of arbitrators who are specialists in class arbitration, and (ii) the parties have the right to appoint the arbitrators, but at least one of them must be from the AAA’s list of arbitrators (in general, the presiding arbitrator).



One of the most important steps in the rules for class arbitrations is the so-called “*construction of the arbitration clause*”, set forth in s. 3. Pursuing this rule, the arbitral tribunal will determine – giving the reasons – whether the arbitration clause permits or does not permit class arbitration. This phase is shaped in the rules as a threshold matter and the arbitral decision, if positive, will take the form of a partial arbitral award (“*clause construction award*”)<sup>112</sup>. JAMS Rules also contain this phase for the construction of the arbitration clause<sup>113</sup>. Following the decision, the arbitral tribunal will stay all proceedings “*for a period of at least 30 days to permit any party to move a court of competent jurisdiction to confirm or to vacate the clause construction award*”. The rules expressly create an opportunity for judicial review of the availability of the class arbitration<sup>114</sup>. As in all other cases, the judicial review of the “*clause construction award*” is limited – it does not allow an *ex novo* review –, subject to the same grounds provided by s. 10 of the Federal Arbitration Act. If any party has sought judicial review, the arbitral tribunal may keep the proceedings suspended until the court decision.

The second most important step in the rules is the so-called “*class certification*”. According to s. 4, the arbitral tribunal will determine the representative parties, who will act in the arbitration “*on behalf of all members of the class*”. Regarding the requirements, the AAA Rules repeats. Rule 23(a) of the Federal Rules of Civil Procedure (a high number of possible class members, questions of law or fact common among the class members, the claims/defences presented by the claimant are typical of the class, and the claimant is an adequate representative party). There is only one further requirement: all members must have entered into a substantially similar arbitration clause. The arbitral tribunal also needs to evaluate whether the class arbitration is superior to other available methods for the fair and efficient adjudication of the controversy<sup>115</sup>. JAMS Rules also provide for this class certification phase (Rule 3(a))<sup>116</sup>.

The arbitral tribunal will render another partial award addressing all these matters described in s. 4. This decision is called in s. 5 a “*class determination award*” and the arbitral tribunal needs to give the reasons for their conclusions. A “*class determination award*” will define the class, the class representative, the class counsel, and also the class claims, issues and defences. All class members will be notified<sup>117</sup> of the “*class determination award*” (s. 6)<sup>118</sup>. This will be an opportunity for class members to opt-out from the class arbitration and pursue their claims individually, otherwise they will be bound by the future arbitral award, as set forth in Rule 6(b)(6)<sup>119</sup>. JAMS Rules provide basically the same in Rule 4(6)<sup>120</sup>. After the rendering of the “*class determination award*”, the arbitral tribunal will stay the arbitration for at least 30 more days to allow any party to seek judicial review<sup>121</sup>. In case of any member seeking judicial review over this partial award, the arbitral tribunal may keep the arbitration suspended until the court decision.

As set forth in s. 7 and 10, the final award must be reasoned, whether or not favourable to the class. Settlements must be approved by the arbitral tribunal to be effective<sup>122</sup>. Mirroring what happens in class actions before courts, all class members must be notified of the proposed terms and the approval of the settlement can only occur after the arbitral tribunal holds a specific hearing on this subject. Class members who disagree with the proposed settlement can opt-out from the class arbitration and pursue their claims on an individual basis, as they will not be bound by the settlement. JAMS Rules regulate final awards and settlements in a very similar way (Rules 5 and 6).

S. 9 regulates the confidentiality of class arbitration. According to the rules, “*the presumption of privacy and confidentiality in arbitration proceedings shall not apply in class arbitrations*” and that “*all class arbitration hearings and filings may be made public*”, with the presence of all interested class members. The AAA also maintains on its website a “*class arbitration docket*” with information about the cases, such as copies of some motions, the identities of the parties, the names of the arbitrators, the names of the counsel, copies of the awards (including the final award<sup>123</sup>), and information about any scheduled hearing (date, time and place). In other words, there is no confidentiality in class arbitrations administered by the American Arbitration Association.

In terms of costs, as regulated in s. 10, the claimant is required to pay USD 3 350 (a “*preliminary filing fee*”) to file a claim, counterclaim or additional claim as a class arbitration. These initial fees will cover all

arbitral institution fees until the rendering of the “clause construction award”. In case of a positive decision, accepting the availability of the class arbitration, a supplemental filing fee – calculated on the basis of the amount in dispute – is required from the claimant. If one of the parties fails to pay the costs, the other one will be notified to pay the amount required.

According to the available database, most of the cases submitted to class arbitration at the American Arbitration Association are related to consumer (37%) or employment matters (34%)<sup>124</sup>. But are shareholders’ disputes also solved by class arbitration in the United States? This review did not identify any cases in practice of class arbitration being used to resolve shareholders’ disputes in the US. In this regard, Gary Born explains that “historically, U.S. courts viewed agreements to arbitrate corporate disputes with disfavour, holding them unenforceable on various grounds”<sup>125</sup>. Chairman Jay Clayton of the Securities and Exchange Commission has stated that “the ability of domestic, publicly-listed companies to require shareholders to arbitrate claims against them arising under the federal securities laws is a complex matter that requires careful consideration” and “if the issue were to arise in an actual initial public offering of a domestic company, it would not be appropriate for resolution at the staff level but would rather be best addressed in a measured and deliberative manner by the Commission.”<sup>126</sup>.

Nevertheless, this *class-arbitration-unfriendly* policy – which is to a good degree informal – appears to have been somewhat softened recently. The District Court in New York, for example, delivered a decision in the case *In re Petrobras Securities Litigation*<sup>127</sup> stating that “the Court is persuaded that, under Brazilian law, Petrobras’ arbitration clause is valid and enforceable against purchasers of Petrobras securities on the Bovespa”. In this regard, District Judge Jed Rakoff remarked that “as a matter of Brazilian law, purchasing Petrobras shares on the Bovespa indicates the purchaser’s consent to be bound by the arbitration clause in the company’s bylaws”<sup>128</sup>. Although the decision was based on Brazilian Law, commentators have seen this case as a positive outcome for the recognition of arbitration for shareholders’ disputes in the US. As James Carter explains, “the decision appears to indicate additional recognition by a US court that mandatory arbitration under corporate bylaws, where provided for under governing law, is not inherently inconsistent with US public policy”<sup>129</sup>.

Finally, it is worth mentioning that the *Financial Industry Regulatory Authority – FINRA* (successor to the *National Association of Securities Dealers – NASD*) operates the largest securities dispute resolution forum in the United States and has extensive experience in solving securities-related disputes. *FINRA* provides two Codes of Arbitration Procedure, one for industry disputes<sup>130</sup> and another for customer disputes<sup>131</sup>. However, according to both Codes, *FINRA* does not administer class arbitrations<sup>132</sup>.

Apparently, the United States do have favourable case law and prepared arbitral institutions, but the use of class arbitrations for shareholders’ disputes has not yet been tested in practice.

Due to the importance of the rules of arbitration of some arbitral institution in dealing with shareholders’ disputes and class arbitration, this chapter summarises the essential information in the table below:

Table 3.1. Main characteristics of the rules of arbitration of the arbitral institutions mentioned in the previous sections

Arbitral institution	Rules for <b>shareholders'</b> disputes	Rules for class arbitration	Appointment of arbitrators	Joinder of third parties	Consolidation	Allocation of costs	Confidentiality	Does the decision bind non-party shareholders?
Deutsche Institution für Schiedsgerichtsbarkeit (DIS)	Yes	No	sole arbitrator and co-arbitrators (but not the president) are appointed by the institution unless parties agree	Yes	Yes	At the discretion of the arbitrators, but Concerned Others who have not joined the arbitration as a party or as an Intervenor are not entitled to reimbursement	Shareholders must be kept informed	Yes
Associação Portuguesa de Arbitragem – APA (proposed rules)	Yes	No	By the arbitral institution if the relief sought by the claimant is the annulment of <b>shareholders'</b> resolutions or if the arbitral decision has the power to bind people who were not formal parties to the arbitration. In other cases, also by the arbitral institution, but here parties are allowed to nominate the arbitral tribunal if they agree on all names	Yes	Yes	Nothing specific, but the general <b>rule is "costs follow the event"</b>	No. Arbitrations must be registered with the registrar of companies and publicised on the <b>company's</b> website	Yes
Corte de Arbitraje de Madrid (CAM)	Yes	No	By the arbitral institution, unless after the disputes arises all parties agree on a different system	Yes	Yes	<b>"costs follow the event"</b>	Yes	Yes
Corte Civil y Mercantil de Arbitraje (CIMA)	Yes	No	By the arbitral institution, unless after the disputes arises all parties agree on a different system	Yes	Yes	<b>"costs follow the event"</b>	Yes, but extracts of the awards can be made public	Yes
American Arbitration Association (AAA)	No	Yes	By the parties	Yes (and also to opt-out)	No specific rule	<b>"American rule"</b> (i.e., parties bear their own costs)	No	Yes
Judicial Arbitration and Mediation Service (JAMS)	No	Yes	By the parties	Yes (and also to opt-out)	No specific rule	<b>"American rule"</b> (i.e., parties bear their own costs)	No	Yes

### 3.11. Considerations about Brazilian Law

As the G20/OECD Principles of Corporate Governance put it, “an important determinant of the degree to which shareholder rights are protected is whether effective methods exist to obtain redress for grievances at a reasonable cost and without excessive delay”<sup>133</sup>. In fact, “policy measures should be designed with a view to their overall costs and benefits, taking into account the need for effective enforcement, including the ability of authorities to deter dishonest behaviour and to impose effective sanctions for violations”<sup>134</sup>.

However, recent studies have shown that the enforcement of shareholders’ rights in Brazil has not been as effective as it could be in terms of standing to sue, remedies, costs, duration of proceedings and economic incentives for the shareholders to litigate<sup>135</sup>. This in a context where publicly held companies raised BRL 450.7 billion in 2019 alone (an increase of 62% between 2018 to 2019)<sup>136</sup> whereas their number has decreased considerably since 1996 (from more than 500 publicly listed companies in 1996 to fewer than 400 in 2019)<sup>137</sup>. Recent scandals followed by widespread public outcry have added a sense of urgency to the need to reform the mechanisms of private enforcement of shareholders’ rights in Brazil.

In this context, it is generally believed that private mechanisms of enforcement of shareholders’ rights need to be further developed in Brazil since, as a study by Cox and Thomas on the American regulatory landscape notes<sup>138</sup>, “*high levels of private litigation can prompt public enforcers to be more active themselves: prosecutors and the SEC risk public criticism if they cannot show that they are doing as much as the private bar. Increased public enforcement, in turn, spurs private litigation that piggybacks on the evidence unearthed*”<sup>139</sup>.

There are of course a number of possible changes to the way Brazilian law regulates securities litigation which could improve its effectiveness, such as easing the requirements on standing to sue under art. 1 of the *Lei 7.913/89* or removing the financial *sword of Damocles* on those who pursue derivative claims embodied by the existing rules on allocation of costs<sup>140</sup>. It is also true that comparative law sounds a note of caution with regard to securities arbitration. Even in arbitration-friendly jurisdictions such as the United States, there is still some reluctance to adopt arbitration as a means of resolving securities disputes – with Spain, as we have seen earlier in this chapter, being one of the few notable exceptions. In the case of the United States, for example, the Securities and Exchange Commission has indeed “*long protected investors from companies’ efforts to force them into mandatory arbitration instead of litigation in federal courts*”<sup>141</sup>.

Nevertheless, Brazilian law has unmistakably opted for arbitration as a means of resolving corporate and securities disputes at least since the reform of the Companies Act in 2001, which expressly acknowledged the validity of *cláusulas compromissórias estatutárias* (see art. 109, §3º, of the *Lei 6.404/76*)<sup>142</sup>. This was reinforced by the creation by the São Paulo Stock Exchange (B3) in the early 2000s of rules of corporate governance mandating arbitration in the context of special listing segments<sup>143</sup>. The legislative reform of 2015 furthered this trend by addressing the right of dissenting shareholders who had opposed the inclusion of an arbitration clause in the articles of association of the company to withdraw from it (see art. 136-A of the *Lei 6.404/76*). Unlike other countries, there is no longer much controversy in Brazil regarding the validity and enforceability of arbitration clauses included in companies’ articles of association (which is why this chapter does not explore this topic in detail).

Brazilian law is now building on its own experience, and that of other jurisdictions, in order to strengthen arbitration as an effective means of enforcing shareholders’ rights in ways that can mitigate the potential risks that its implementation may present – with regard, for example, to transparency and adequate supervision by the markets regulator.

The way Brazilian law evolved over the course of the last years in terms of the emphasis it puts on the role of arbitration as the preferred means of resolving corporate and securities disputes is definitely unique in the landscape of comparative law. There are impressive data showing that an important part of the caseload of the Brazilian arbitral institutions is comprised of internal companies’ disputes.

As regards B3's *Câmara de Arbitragem do Mercado* ("Market Arbitration Chamber"), almost 70% of the cases administered by the institution from 2010 to 2019 were related to shareholders' disputes. In 2019, according to the data provided by e-mail<sup>144</sup>, the arbitral institution received 27 new requests for arbitration, 59% of them dealt with internal company disputes, including 2 class arbitrations<sup>145</sup>.

In 2013, an internal survey carried out by the *Centro de Arbitragem e Mediação da Câmara de Comercio Brasil-Canadá* ("Centre for Arbitration and Mediation of the Chamber of Commerce Brazil-Canada", CAM-CCBC) revealed that 28.89% of the cases commenced in that year dealt with shareholders' disputes. In 2018, 40% of the new cases (101 in total) were corporate arbitrations<sup>146</sup>, and in 2019, the percentage reached 51% (49 out of 97 new cases)<sup>147</sup>, which shows a remarkable increase in the number of cases related to internal company disputes.

As for the *Câmara de Conciliação, Mediação e Arbitragem de São Paulo – Ciesp/Fiesp* ("Chamber of Conciliation, Mediation and Arbitration of São Paulo – Ciesp/Fiesp"), the percentage of arbitrations related to corporate issues was 24.39% in 2015; 22.81% in 2016; 30.61% in 2017; and 25% in 2018<sup>148</sup>. On average, more than a quarter of the new cases discussed corporate matters.

The *CAMARB – Câmara de Arbitragem Empresarial – Brasil's* docket ("CAMARB – Business Mediation and Arbitration Chamber-Brazil") shows that 20% of new cases administered by the arbitral institution between 2018 and 2019 were related to shareholders' disputes<sup>149</sup>.

In the case of the *Centro de Arbitragem e Mediação AMCHAM* ("Centre for Arbitration and Mediation AMCHAM"), the rate of new arbitrations involving disputes company-shareholders and shareholders-shareholders reached 16% in 2018 and 17% in 2019 (from 2010 to 2019, the average percentage was 18.9%)<sup>150</sup>.

Furthermore, it is important to highlight that São Paulo's Stock Exchange created in 2000 what is called the "New Market", which is a listing segment of the stock exchange market for companies that comply with high levels of corporate governance. One of the requirements to be accepted in the "New Market" is the inclusion of an arbitration clause in the company's articles of association. Such requirement was extended to other segments of the stock exchange. The initiative was successful in Brazil, as many public companies have decided to enter into the "New Market". Moreover, according to Mariana Pargendler, Viviane Muller Prado and Alberto Barbosa, 27% of the companies listed on "Básico" and "Nível 1" segments of B3 (Sao Paulo Stock Exchange) adopt mandatory arbitration clauses in their articles of association (15%) or in their shareholders' agreement (16%)<sup>151</sup>. It is relevant to note that in such segments companies are not obliged to do so since they are only mandatory for those listed on "Bovespa Mais", "Bovespa Mais Nível 2", "Novo Mercado" and "Nível 2" segments. Rather, they have chosen arbitration voluntarily as the most suitable method of dispute resolution.

### **3.11.1. Lessons from other jurisdictions**

Although Brazil already makes much wider use of arbitration for the resolution of shareholder disputes than the other nine jurisdictions reviewed for this chapter, the experience and legal frameworks of these jurisdictions can provide the basis for a number of useful insights which could help Brazil to improve its own system of enforcement. It is important to highlight that there is no legal system that provides for class arbitration involving shareholders' disputes in publicly-held companies. There are legal systems with a sophisticated class action framework, but which cannot be applied to arbitration (e.g. Israel). Some other countries have a well-developed class arbitration system, but which has not been tested in corporate cases (e.g., the US). There are other cases in which arbitration is available for corporate disputes, but only for individual claims, not collective claims (e.g., Spain). There are also those which have arbitration involving corporate disputes, but not for publicly-held companies (e.g., Germany). Some jurisdictions provide useful insights from legal documents of arbitration chambers or supplementary rules (Germany, Spain, US), while the case of Portugal, draft legislation raises relevant issues for consideration. Last but not least, some

jurisdictions simply do not have collective redress (e.g., the UK, except for competition issues, and Singapore). In this chapter, the useful insights abovementioned come from different sources, i.e., different systems.

*First*, French and Spanish scholars are right to point out that the arbitrability of disputes between companies and their shareholders is not adversely affected by the circumstance that they involve public order rules or rights of multiple parties<sup>152</sup>. In this regard, art. L721-3 of the French *Code de Commerce* is very similar in scope to art. 109, §3º, of the Brazilian Companies Act although the wording of art. 11-b of the Spanish *Ley de Arbitraje* leaves less room for ambiguity. Besides, art. 136-A of *Lei 6.404/76* is not unconstitutional under Brazilian law because a majority of shareholders have the power to make decisions that bind the entire group of shareholders (majority principle) while recourse to arbitration is by no means a second class mechanism of access to justice under art. 5, XXXV, of the Constitution<sup>153</sup>. Access to arbitration is access to justice, as already declared by the Brazilian Supreme Court<sup>154</sup>. Finally, shareholders are fully aware of the arbitration clause in the articles of association before becoming members, which means that those shareholders who do not want to be bound by an arbitration agreement always have the option to not become a member (and, hence, to buy shares or invest money in another company).

*Second*, German and Italian authorities are right to caution against the dangers to due process that arbitrations involving shareholders may present insofar as they emphasize the importance of *procedural* safeguards against the violation of shareholders' right to be heard before a final decision is made against them. In fact, the issue as to whether shareholders are validly bound to the agreement to arbitrate under the articles of association is entirely different from the strictly *procedural* issue as to whether a shareholder who had not been party to the arbitral proceedings may be deemed lawfully bound by the award.

The German *Bundesgerichtshof* (BGH) addressed this issue in the landmark case *Schiedsgerichtbarkeit II* (Arbitrability II) and ruled that – notwithstanding the lack of express statutory authorisation to this effect – shareholders of a limited liability company are free to agree to be bound by an arbitral award related to the validity of shareholders' resolutions<sup>155</sup> *provided* that some procedural safeguards are in place.

According to the German court, “all shareholders consented to arbitration either through an arbitration clause in the articles of association or by separate agreement; all stakeholders, i.e., all shareholders, managing directors, and members of the supervisory board, if any, must be notified of the institution of the arbitration and be constantly updated about the arbitration and be granted a fair opportunity to actively participate in the proceedings; all stakeholder must have an equal opportunity to participate in the constitution of the tribunal; all disputes regarding a specific shareholder resolution must be concentrated in one single arbitration to exclude conflicting decisions”<sup>156</sup>.

It was this ruling that led the Deutsche Institution für Schiedsgerichtsbarkeit (DIS) to enact “supplementary rules for corporate disputes” so that arbitration under its Rules could fulfil the requirements set forth by the BGH. The same approach of procedural safeguards is easily identified in the AAA Supplementary Rules for Class Arbitrations and in the JAMS Class Action Procedures. We will return to these procedural safeguards shortly<sup>157</sup>.

Third, some American commentators worry justifiably that confidential arbitral proceedings in corporate and securities matters carried out without supervision either by the markets regulator or the courts might frustrate the positive externalities that litigation would be more likely to produce.

In fact, according to this line of reasoning, “the resolution of private disputes in public courts creates positive externalities. In other words, the public also benefits when private litigants use courts because a public hearing gives judges a chance to tell corporate insiders what the law expects of them. Holding wrongdoers to account tells the public that we take corporate fraud seriously — and sends a signal to insiders, the bar, and investors, that being unfaithful to investors doesn't pay. Arbitration, on the other hand, is usually conducted in a closed-door proceeding, depriving investors of their chance to air their objections — and

the rest of us the knowledge of what the law is”<sup>158</sup>. Nevertheless, as we shall later see, changes to rules related to confidentiality, publication of sections or redacted versions of awards and some degree of supervision by the CVM of the proceedings may contribute to allay these legitimate concerns.

*Finally*, the large use of class arbitrations in the United States — where the Federal Arbitration Act is silent on the subject — suggests that the rules of arbitral institutions such as those from the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS)<sup>159</sup> are perhaps better suited than statutory provisions to regulate in detail how proceedings in class arbitrations should be carried out, because the applicable rules can be more easily changed and adapted when needed while arbitral institutions are also more responsive than lawmakers to the feedback provided by users of the service.

### **3.11.2. Arbitrability and agreement to be bound by the result of the arbitration**

Disputes among publicly listed companies and their shareholders, as we have seen earlier, are arbitrable under Brazilian law for the same reasons in countries such as France and Spain<sup>160</sup>. The arbitrability of such internal company disputes are indeed recognised in most of the nine selected jurisdictions.

Moreover, shareholders are also bound to arbitrate under Brazilian law if the articles of association so provide on the basis of applicable rules of contract and commercial law (so-called *cláusula compromissória estatutária*)<sup>161</sup>. Undisputedly, art. 136-A of *Lei* 6.404/76 expressly allows this. But can shareholders who are third parties to arbitral proceedings between the company and other shareholders — albeit privy to the arbitral agreement — be bound by the award rendered *inter alios*? For some scholars, due process would not allow it<sup>162</sup>. This chapter takes a different view.

Under Brazilian law, shareholders may agree beforehand not only to arbitrate but also to be bound by an award rendered in proceedings to which they are not parties, provided some procedural safeguards in their benefit are in place. To clarify: “beforehand” means at the outset of the case (which is related to the safeguards detailed below). Therefore, it is not necessary to pass a resolution to include a specific provision allowing class arbitration in the companies’ articles of association. The existing arbitration clauses inserted in many companies’ articles of association in Brazil work as sufficient legal source to permit the resolution of corporate disputes through arbitration, either on an individual basis, or on a collective basis. The reasons for this are simple: (i) the shareholder is not entitled to two distinct rights, one individual and another collective, and (ii) there are not two types of arbitration clauses, one for individual arbitrations and another for collective arbitration.

This is precisely what art. 11.1 of Annex 5 of the Germany’s DIS Rules means when it provides that “the shareholders designated as Concerned Others within the provided time limits agree to recognize the effects of an arbitral award rendered in accordance with these DIS-CDR”. We may call this approach, therefore, the German approach applied to publicly listed companies<sup>163</sup> which lies within the framework Setoguti refers to as “autorregulação processual” (i.e. procedural autonomy). The advantages of this approach are numerous. Most importantly, as the German BGH explains in the case *Arbitrability II*, it enables so far as possible the concentration of the proceedings in one single arbitration as to avoid conflicting decisions and endless and costly parallel litigation (*Verfahrenskonzentration*)<sup>164</sup>.

In the United States this approach is broader as it applies not only to shareholders’ disputes – although these disputes are normally resolved by state courts – but also to conflicts related to consumer and employment matters. As abovementioned, the AAA Supplementary Rules for Class Arbitrations<sup>165</sup> and the JAMS Class Action Procedures (Rule 4(6))<sup>166</sup> establish rules by which third parties are bound by the arbitral award rendered in class arbitration. Therefore, when the parties agree with the arbitration clause and, hence, with the rules of arbitration mentioned in the clause, they automatically agree to be bound by arbitral awards rendered in class arbitration subject to those rules of arbitration.

Based on these experiences formulated by German and American arbitral institutions, we conclude that the rules of arbitration of the arbitral institutions can establish the extension of the effect of the arbitral

awards (*intra societatem* effect, as it is explained below) over those shareholders who did not act as formal parties in the class arbitrations, provided they had agreed with the rules previously. There is no need to pass a resolution to include a specific provision allowing class arbitration in the companies' articles of association. The legal systems, however, are required to ensure certain safeguards, as we describe below.

### **3.11.3. Freedom of contract and *intra societatem* effects of the arbitral award**

Freedom of contract — in the civil law sense of *autonomia privada*, *Privatautonomie*, *autonomie de la volonté* — is a founding principle of Brazilian arbitration law<sup>167</sup>. And it is on the grounds of this principle that parties may agree not only to arbitrate disputes which are arbitrable but also to dispose of so-called “*direitos patrimoniais disponíveis*” (negotiable and pecuniary rights). *A fortiori*, freedom of contract equally calls for the parties to agree to abide by an arbitral award rendered *inter alios* concerning alienable rights if they so wish, and provided some procedural safeguards are in place. This is the essence of the German approach to *erga omnes* effects of arbitral awards<sup>168</sup>.

The freedom of contract is also the fundamental reason behind the case law built by the US Supreme Court to allow class arbitration. As the Court established in *American Express Co. v. Italian Colors Restaurant*, “arbitration is a matter of contract”, which means that courts must “rigorously enforce arbitration agreements according to their terms”<sup>169</sup>. According to this understanding, if the parties to the arbitration agreement agree to be bound by an arbitral award rendered in class arbitration, it is a matter of contract and, therefore, must be recognised and enforced by courts.

In practical terms, it is essential to define when and how parties should agree to be bound by an arbitral award rendered in class arbitration. Should the articles of association contain a specific provision allowing class arbitration? Should parties write a specific clause in the arbitration agreement stating they consider themselves bound by any class arbitration award? Would it be enough to refer to institutional rules of arbitration containing class arbitration provisions? In other words, the question is: when and how will parties exercise their freedom of contract in such a scenario? The authors of this chapter take the view that the provision stating that parties will be bound by the class arbitration award should be contained in the institutional rules of arbitration adopted by the parties. In this case, the company's articles of association have to refer to such institutional rules of arbitration.

It is worth noting, nevertheless, that the commonly used expression *erga omnes* effects is something of a misnomer in this context because it suggests that the award could be binding “towards all” — this is precisely the literal translation of the Latin expression *erga omnes* — and not only to those who had been privy to the arbitral agreement. In reality, it may bind only those who had agreed to be bound because “*no one shall be obliged to do or refrain from doing something except by virtue of law*” (Constitution, art. 5, II). In this sense one may describe the extension of these effects as *intra societatem* (“inside the company”) because they bind only those who agreed to be bound by virtue of the arbitral clause contained in the articles of association (*autorregulação processual* - procedural autonomy).

### **3.11.4. Procedural safeguards: notice, right to intervene, formation of the arbitral tribunal, settlements, right to opt out, consolidation, supervision by the CVM, publicity of the awards, binding effects and cost allocation**

*Intra societatem* effects of arbitral awards, as we have seen, may only bind those who are privy to the arbitral agreement (as per the *cláusula compromissória estatutária*) if some procedural safeguards are in place.

First, shareholders must be given proper and timely notice of the initiation of the arbitration and its subject matter. This is a *procedural* requirement under the constitutional and statutory guarantee of due process and not a *substantive* duty under the applicable securities regulations (so-called *fato relevante*)<sup>170</sup>.



The right to be informed about the commencement of a class arbitration, for instance, is expressly provided by the AAA Supplementary Rules for Class Arbitrations (Rule 6)<sup>171</sup>, which states that the class members must be provided “the best notice practicable under the circumstances”. The same requirement can be found in the JAMS Class Action Procedures (Rule 4)<sup>172</sup>. To some extent, this is also the approach taken by art. 2.1 of Annex 5 of the *Deutsche Institution für Schiedsgerichtsbarkeit* (DIS) Rules of 2018; art. 35, para. 1, of the Italian *Decreto Legislativo* 5 of 2003; art. 4 of the Bill drafted by the Portuguese *Secretaria de Estado da Justiça* in 2018; and s. 5(4) of the arbitration rules drafted by the *Associação Portuguesa de Arbitragem – APA*.

In practical terms, this chapter suggests two ways to ensure shareholders’ rights to be informed: (a) the company concerned can issue a Material Fact informing its shareholders and the market regarding the commencement of a class arbitration, and (b) the company concerned can notify all its shareholders by e-mail. In addition, the CVM can provide a space on its website where all class arbitrations would be listed. In the view of this chapter, such initiatives do not require any legislative modification. The CVM could regulate such initiatives by issuing a regulatory act (e.g., “Instrução Normativa”).

*Second*, shareholders – and third parties – must be granted a fair opportunity to participate in the proceedings in general and in the constitution of the arbitral tribunal in particular<sup>173</sup>. Again, AAA Supplementary Rules for Class Arbitrations specify in Rule 6(b)(4) that “a class member may enter an appearance through counsel if the member so desires, and that any class member may attend the hearings”. The JAMS Class Action Procedures provide exactly the same right (Rule 4(c)). The same rationale can be found in 2.1 of Annex 5 of the *Deutsche Institution für Schiedsgerichtsbarkeit* (DIS) Rules of 2018; art. 35, para. 2, of the Italian *Decreto legislativo* n.5 of 2003; s. 52(5) of the rules of arbitration of the *Corte de Arbitraje de Madrid*; and s. 68(5) of the rules of arbitration of the *Centro de Arbitraje Internacional de Madrid* (CIAM).

Regarding the formation process of the arbitral tribunal, the systems we have examined offer different solutions. In Italy, according to art. 34, para. 2, Decreto Legislativo 5 of 2003, the arbitral tribunal is to be appointed by a person or institution external to the company. In Portugal, the arbitration rules drafted by the *Associação Portuguesa de Arbitragem – APA* in 2016 establish that, as a rule, the sole arbitrator or the members of the arbitral tribunal will be appointed by the arbitral institution, unless the parties agree on the name(s) of the arbitrator(s) (s. 5(1) and (2)). However, the arbitral institution will appoint the arbitrator(s) if the relief sought by the claimant is the annulment of shareholders’ resolutions or if the arbitral decision is capable of binding people who were not formal parties to the arbitration (s. 5(3)).

In Spain, s. 52(3) of the rules of arbitration of the *Corte de Arbitraje de Madrid* establishes that arbitrators will be appointed by the Court (unless, after the dispute arises all parties agree on a different system). Similar provisions can be found in s. 4(3) of the rules of the *Corte Civil y Mercantil de Arbitraje* (CIMA) and in s. 68(3) of the rules of the *Centro de Arbitraje Internacional de Madrid* (CIAM). The Spanish system, as provided by the institutional rules of arbitration, leaves some room for the parties to choose the arbitrators. In the US, according to the American Arbitration Association’s rules of arbitration, the parties have the right to appoint the arbitrators, but at least one of them must be from the AAA’s list of arbitrators (s. 2).

Taking into account the practice in Brazil, this chapter suggests that the process of appointing arbitrators should follow the rules applicable to all arbitrations, as set forth in the relevant institutional rules of arbitration. The general rule according to which parties choose their arbitrators, and the co-arbitrators appoint the presiding arbitrator, seems suitable for class arbitration as well. The authors of this chapter do not identify major problems regarding this general rule in Brazilian arbitration.

This suggestion gives rise, however, to legitimate concerns. The most important one is that, by adopting that suggestion, a shareholder who is not formally a party to the arbitration (but who will be bound by the final award) will not have the right to choose the arbitrator. Nonetheless, the alternatives are also problematic. Since it is impossible to grant to all shareholders the right to choose the arbitrator, a reasonable solution is to empower the arbitral institution to choose the arbitrators on behalf of the parties.

That alternative, however, raises new issues. Firstly, empowering the arbitral institution to choose the arbitrator does not mean that shareholders will have any influence on that choice. As a result, they will continue to be subject to an arbitrator who was not chosen by them. Secondly, empowering the arbitral institution to choose the arbitrator means that the minority shareholders' side will lose the right to choose one arbitrator. So, instead of increasing the power of the minority shareholders, it will by contrast reduce their power in the arbitration. Thirdly, if there is any concern regarding potential collusion between the shareholder who has chosen the arbitrator and the company, it is a matter for civil and criminal liability. The authors of this chapter do not recollect any reported cases of collusion between parties in arbitrations in Brazil, which is why such concerns should not drive our initiatives.

The opportunity to participate in the proceedings is also applicable in case of settlement, where shareholders must be given the right to opt-out if they disagree with the proposed terms (Rule 8 of the AAA Supplementary Rules for Class Arbitrations, and Rule 6 of the JAMS Class Action Procedures, Rule). In practical terms, they should be informed about the terms of the proposed settlement, following the same rules established to make them aware of the commencement of the arbitration (as described above).

*Third*, shareholders must have the right to opt out from the arbitration if they so wish. In this case, the rules of arbitration of the arbitral institution should define specific opportunities and the corresponding time periods for that. This chapter takes the view that the opt-out proceedings are the most efficient and fair system of collective redress. Provided the shareholders are fully informed of the commencement the class arbitration (as suggested above), there is no reason to mistrust the opt-out system. It is worth highlighting that the most effective jurisdictions in the world in terms of class actions adopt such a rule, as is the case in the United States and Israel.

It's worth noting that the specific rules regarding class arbitration will only govern arbitrations related to rights arisen after (not before) its incorporation to the rules of arbitration of the arbitral institution (and it must be clearly stated in the rules). As part of the companies' duty to inform, companies should notify their shareholders about the new rules of class arbitration and let them know that any collective redress started from that point in time (= rights arisen from that point in time) will follow such new rules.

Specifically to arbitration, the AAA Supplementary Rules for Class Arbitrations and the JAMS Class Action Procedures make clear that shareholders have two opportunities to exercise their right to opt-out: (i) after being notified of the commencement of the class arbitration (Rules 6(b)(5); and Rule 4(5)) and (ii) after being notified of the purposed terms of a settlement (Rule 8(c); and Rule 6(c)). This report suggests that arbitral institutions should issue special rules for class arbitration contemplating such opt-out proceedings. As explained above, the authors of this chapter understand that no legislative alteration is necessary as parties are allowed to agree to be bound in opt-out proceedings.

In practical terms, shareholders should be notified of the commencement of the class arbitration and should also be given the opportunity to inform the arbitral institution – within a certain period of time, v.g., 45 days, as in Israeli class actions – if they do not want to be included in the case. Once this time limit expires, all shareholders should be considered to have agreed to be bound by the future class arbitration award.

As for consolidation, considering that the report suggests opt-out proceedings and also specific rules to permit the participation of other shareholders and third parties, the recommended practice is that the first request for arbitration should prevent further requests from being filed by other claimants. In this case, other claimants should be allowed to join the first request for arbitration. This is the approach taken in Spain by the *Corte Civil y Mercantil de Arbitraje (CIMA – s. 4(5))*, the *Centro de Arbitraje Internacional de Madrid (CIAM – s. 68(6))* and the *Corte de Arbitraje de Madrid (s. 52(6))*. After the appointment of the arbitral tribunal of the first arbitration, consolidation should only be acceptable if all the parties involved agree to the request for joinder, as established in s. 52(6) of the *Corte de Arbitraje de Madrid's* rules of arbitration.

*Fourth*, as a consequence of the opt-out proceedings, the class arbitration award should bind all shareholders, regardless of their formal participation or intervention in the arbitration, and regardless of its content (whether it benefits the shareholders or not). This is, for example, the provision set forth in s. 10(1) of the Bill drafted by the Portuguese *Secretaria de Estado da Justiça* in 2018. In the same sense is s. 212 of the Israeli Companies Law 1999 for class action involving corporate arbitrations. As explained by commentators (mentioned above), this is also the rule in Spain, where the arbitral award shall be binding on all shareholders, regardless of whether they have taken part in the arbitration or not.

Again, the authors of this chapter believe that it is not necessary to change any statute to incorporate the binding effect of the class arbitration award in the Brazilian arbitration, provided that (i) the institutions' rules of arbitration set out provisions on this regard, and (ii) the safeguards recommended in this item of the chapter are also adopted.

*Fifth*, the collective nature of the dispute may justify the supervision of the proceedings by the CVM under art. 31 of *Lei 6.385/76*. In practical terms, the rules of arbitration of the arbitral institution should empower the arbitral tribunal to notify the securities and exchange authority of the commencement of the arbitral proceedings. This is the practice in Israel for class actions, where the *Israel Securities Authority (ISA)* participates in the judicial process by giving its opinion (s. 19(b)(4)). This rule can be easily replicated in class arbitration in Brazil. In practice, the special rules for class arbitration should contain a provision establishing the exact moments in which the arbitral tribunal should notify the CVM. This chapter suggests that the CVM should be given notice of (i) the commencement of the case, (ii) the terms of reference, (iii) the terms of any proposed settlement, (iv) the hearings, and (v) the decisions made by the arbitral tribunal. The effectiveness of these recommended measures largely depends on the CVM structure, in particular its staff.

Sixth, sections or redacted versions of arbitral awards related to collective arbitrations should be published — as they are at the time of publication, for example, under the Rules of the *Câmara de Arbitragem do Mercado*, Rule 7.10 — as to mitigate to a certain extent the effects of confidentiality as well as to achieve the positive externalities hailed by some commissioners of the American SEC as mentioned above.

According to Rules 9 and 10 of its Supplementary Rules for Class Arbitrations, the AAA maintains on its website a “class arbitration docket” with information about the cases, such as copies of some motions, the identities of the parties, the names of the arbitrators, the names of the counsel, copies of the awards and information about any scheduled hearing (date, time and place) insofar as the nature of the disputes and the precedential force of the awards might be clearly understood. As for the *Corte Civil y Mercantil de Arbitraje* in Spain, its rules of arbitration impose publicity on arbitral awards (with the disclosure of the names of the arbitrators – s. 63(1)). In order to increase accountability, this chapter suggests that arbitral awards should be made public, including the names of the arbitrators.

*Seventh* and finally, as for costs, the survey conducted in several jurisdictions shows that class arbitrations follow the general cost-allocation scheme, i.e., “costs follow the event”. This means that the costs of an arbitration are usually awarded to the winning party and, therefore, the losing party needs to reimburse the winning party for all the costs incurred (arbitrators' fees, arbitral institution's fees, administrative expenses etc).

In Spain, the rules of the arbitral institutions adopt an approach of “costs follow events” (unless the parties agree otherwise), mirroring the rules found in the Spanish Civil Procedure Code. In this sense, the rules of the *Corte de Arbitraje de Madrid* (s. 40(6)), the *Centro de Arbitraje Internacional de Madrid* (s. 45(7)) and *Corte Civil y Mercantil de Arbitraje* (s. 46(3)). In the US, the AAA Supplementary Rules for Class Arbitrations adopt the same rule, as set forth in its s. 10, even for consumer and employment class arbitrations.

This chapter considers the rules regarding cost allocation an important issue in shareholders' disputes, as they can work as positive or negative economic incentives for the use of arbitrators to resolve shareholders

disputes. In legal systems that adopt the “costs follow the event” rule (as in the Brazilian system), the amount of costs has a particular influence on the decision to file new claims. On the one hand, if the costs are high and the claimant can be found liable for such costs, the claimant will only start a new case if it considers its chances of success to also be high. If the claimant is not entirely sure, it will prefer to solve the dispute by other low-risk means, such as negotiation or mediation. It is worth noting that if the costs are too high, it can prevent the claimant from bringing even well-founded claims. On the other hand, if the costs are low – or there are no costs at all –, the claimant will start the case regardless of its chances of success. The reason for this is simple: there is no adverse risk, i.e., nothing to lose.

Legal systems should carefully consider such positive and negative effects in order to find a reasonable balance in each field. Such reasonable balance depends on the field concerned. As is self-evident, such balance can be very different in disputes related to consumer matters and in disputes related to corporate matters. In shareholders’ disputes, high costs create a negative incentive for minority shareholders to pursue their rights against the company or the controlling shareholders. In turn, low costs create a positive incentive for minority shareholders to commence legal proceedings against the company or the controlling shareholder, which in some cases can end up in minority abuse, i.e., the use of legal proceedings against every resolution or every decision made by the board with the ulterior purpose to increase their bargaining power in the company.

The authors of this chapter understand that in class arbitrations the cost allocation should follow the same rules applicable to all other arbitrations. Furthermore, the cost allocation in class arbitrations should adopt the “costs follow the event” rule. This is the practice adopted in other jurisdictions regarding class arbitrations (even in consumer and employment matters) and arbitrations involving shareholders’ disputes. No legal or regulatory initiatives are necessary. The authors of this chapter, however, recommend that the rules of arbitration of the arbitral institution establish a pre-trial stage to evaluate whether the claim is meritorious or not. The leading shareholder should bear the costs incurred between the commencement of the class arbitration and the decision taken at the end of the pre-trial stage (such costs should be fixed in a reasonable amount). If the claim is considered meritorious, then the company should bear the costs from this moment onwards until the delivery of the final award.

*Eighth* and finally, among the legal systems investigated, the American system is the only one which allows the arbitral institution to choose the counsel who will conduct the class arbitration. This possibility is in line with the legal framework for class actions (before courts) in the United States. However, there is no such possibility in any other country investigated, neither in Civil Law countries, nor in other Common Law countries. The authors of this chapter understand that parties should be granted the freedom to choose their counsel. In addition, the authors of this chapter do not recollect any problems related to the choice of counsel in arbitrations or court proceedings, even in cases between companies and consumers, and employers and employees. Finally, there is no guarantee that a third-party would be able to choose a better counsel than the party who holds the rights *sub judice*. It should be noted as well that any political influence must be kept apart from class arbitration, which could happen if an institution were in charge of the nomination of the counsel.

### **3.11.5. Legal reform: Institutional rules and secondary legislation**

Under German law a specific legislative authorization is not necessary for companies and shareholders to execute an agreement to be bound by the arbitral award — on the basis of the parties’ autonomy (*Privatautonomie*) — so that a provision under the articles of association would suffice according to the BGH (Arbitrability II). Similarly, class arbitrations are not expressly mentioned by the Federal Arbitration Act 1925, the Securities Act of 1933 and the Securities and Exchange Act of 1934, so that it is essentially institutional rules which regulate in the United States how they are carried out.

The same rationale applies to Brazilian law on the grounds of *autonomia privada* (freedom of contract) as the notion is construed under art. 5, II, of the Constitution, and art. 1 of the Arbitration Act. Moreover, it is

equally not necessary that the arbitral agreement expressly provides for the *intra societatem* effects of the arbitral award if the institutional rules to which it refers regulate the matter on the grounds that “*when parties agree to arbitrate under institutional rules, they are deemed to have incorporated those rules into their agreement, and are therefore bound by such rules as a contractual matter*”<sup>174-175</sup>. This provision works as a “*convenção processual*” (procedural agreement). As per Art. 5 of the BAC provisions, institutional rules are binding on the parties.

For the sake of legal certainty, nonetheless, the Brazilian Arbitration Act could be also amended in order to dispel doubts about the legality of this type of agreement under which someone agrees to be bound by an arbitral award rendered in proceedings to which he or she was not a party. *À propos*, preclusive effects of judgments for non-parties are already lawful under Brazilian law as per art. 506 of the Brazilian Code of Civil Procedure if the judgement has been rendered *in favour* of the third party (both defensive and offensive one-way preclusion)<sup>176-177</sup>. Nothing bars the parties from contracting out of the mutuality rule if they so wish in relation to disputes that are arbitrable under Brazilian law. In practical terms, a single legal provision could establish that parties are free to solve their corporate disputes through class arbitration according to the rules of arbitration adopted by the company in its articles of association, which could provide for opt-out proceedings and binding effect of the arbitral award.

Furthermore, there is ample room under Brazilian law for the CVM to regulate the extent to which the procedural safeguards alluded to earlier satisfy the demands of due process and of protection of the securities market as a whole in terms, for example, of how notice of arbitral proceedings should be carried out, the conditions under which CVM's intervention as *amicus curiae* might be necessary, or communication of outcomes of arbitrated cases. Some of the concerns voiced by American authorities also could be allayed by means of corporate governance rules and secondary legislation, for example, with regard to the inadmissibility of class arbitration waivers<sup>178</sup>.

### 3.11.6. Specific rules for collective arbitration

Legislation should not govern how arbitral proceedings are conducted, as this is essentially a matter for the parties and institutional rules (where the parties opt for institutional arbitration) to decide. In our opinion, nonetheless, arbitral institutions should create specific rules for collective arbitration in light of the challenges that an originally “*dual-party design*”<sup>179</sup> may pose in terms, for example, of how arbitrators are appointed by the parties.

Rules of American arbitral institutions such as those from the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS) are an obvious source. In this regard, Rules 23 and 23.1 of the American Federal Rules of Civil Procedure on class actions present a good template from which Brazilian arbitral institutions could draw inspiration. For example, the template may help in ensuring consideration of the adequacy of representation in the appointment of a class representative, the subdivision of classes, and approval by the arbitrators of any settlement or voluntary dismissal.

Finally, arbitral institutions and regulators could establish special rules concerning allocation of costs in securities matters — diverging from those applicable to securities litigation before state courts — so that they may serve as an economic incentive for shareholders to seek redress on their behalf and, even more importantly from a regulatory point of view, on behalf of the company.

## 3.12. Conclusions

Brazil and Spain are the only jurisdictions among the 10 jurisdictions covered in the present comparison that have clearly opted for arbitration as a means of resolving corporate and securities disputes involving publicly listed companies. However, in addition to the rules and practices adopted by Spanish institutions, other jurisdictions may serve as a source of experience to be considered in the Brazilian context.

In one arbitration institution in Germany and two others in the US covered by the chapter, the publicity of the main phases of an arbitration proceeding is a necessary – though not sufficient – condition for the existence of collective arbitrations involving the enforcement of shareholders' rights (in Germany, the rules mentioned here are for non-listed companies, since disputes over collective rights of minority shareholders of publicly held companies are not arbitrable in mentioned country). Moreover, the opt-out system adopted in the US for class actions might also be a potential benchmark for collective arbitrations in Brazil.

Although Brazil has made greater use of arbitration than other reviewed jurisdictions to address disputes among publicly listed companies and their shareholders, this chapter nevertheless concludes that further steps could be taken to enhance its use, particularly for collective shareholder actions. The following chapter authored by Guilherme Setoguti will review in more detail the rules and practices of corporate arbitration in Brazil, and propose changes to the existing framework, taking into account insights and potential lessons from the experience of other countries reviewed for this chapter.

Recent studies have shown that the enforcement of shareholders' rights in Brazil has not been as effective as it could be. In this context, we are convinced that collective arbitration could be more effectively employed in Brazil — without the need of any legislative modification — as a means of enforcing shareholders' rights. One important step to increase the effectiveness of collective arbitration in Brazil would be the wide adoption of the opt-out system, which is, according to the previous analysis, the most efficient and fair system for collective redress.

Under Brazilian law, disputes among publicly listed companies and their shareholders have been arbitrable for many years. As shareholders are bound to arbitrate if the articles of association provide for this, it is our understanding that rules of arbitral institutions can provide for class arbitration if some procedural safeguards are observed.

These procedural safeguards concern, in essence, the shareholders' right to be notified of the arbitral proceedings and to have a fair opportunity to participate in the proceedings in general and in the constitution of the arbitral tribunal in particular (or to opt-out if they so wish). We also believe that the collective nature of the dispute may justify the participation in the proceedings by the CVM as an *amicus curiae* and its regulation of the transparency that should be provided by public companies on the existing proceedings.

## Notes

<sup>1</sup> Of Counsel at Quinn Emanuel Urquhart & Sullivan LLP (London office). Visiting Scholar at the School of International Arbitration at Queen Mary – University of London (2018-2019). Junior Academic Visitor at the University of Oxford (Commercial Law Centre – Harris Manchester College, 2015-2016). PhD's Degree in Civil Procedural Law from Pontifical Catholic University of São Paulo (2013-2017). Master's Degree in Civil Procedural Law from Pontifical Catholic University of São Paulo (2009-2012). Bachelor's Degree in Law and Social Sciences from the Law School of Federal University of Rio de Janeiro (2000-2005). Brazilian qualified lawyer (São Paulo and Rio de Janeiro). Contact: [andremonteiro@quinnemanuel.com](mailto:andremonteiro@quinnemanuel.com) .

<sup>2</sup> Professor of Civil Procedure at the Pontifícia Universidade Católica do Rio de Janeiro (PUC-RIO). Partner at Sergio Bermudes Advogados. Promotion (Ph.D.), Ruprecht-Karls-Universität Heidelberg, Germany. Mestrado (Master of Laws), Universidade de São Paulo (USP), Brazil. Graduação (LL.B.), Pontifícia Universidade Católica do Rio de Janeiro (PUC-RIO), Brazil. Visiting Fellow at the University of Oxford (academic visitor; Institute of European and Comparative Law), England, 2014. Ricercatore post-

dottorato at the Università degli Studi di Firenze, Italy, 2016. Gastwissenschaftler at the Ludwig-Maximilians-Universität München, Germany, 2018. Contact: [beneduzi@puc-rio.br](mailto:beneduzi@puc-rio.br).

<sup>3</sup> References to data in this chapter were last updated on 14 July, 2020

<sup>4</sup> The Latin expression *amicus curiae* (literally, friend of the court) means a person or group who is not a party to legal proceedings or arbitration but is allowed by law to intervene in the case and submit a brief with the intent of influencing the decision of the court or arbitral tribunal. To be admitted, the *amicus curiae* needs to prove it has an institutional interest in the subject matter. Normally, the *amicus curiae* is an institution which provides data, surveys or technical information that will help the court or the arbitrators to understand the impact of their decision on the community or a specific market.

<sup>5</sup> The Latin expression *res iudicata* (or *res judicata*) means the binding effects that cover a matter already decided by a judge or an arbitrator. Normally, this effect covers the relief requested and/or the cause of action, depending on the applicable law. Once such a matter has been adjudicated, parties cannot repeat the same claim in another legal proceeding or arbitration. In Common Law countries, *res judicata* is also called claim preclusion.

The Latin expression *erga omnes*, in this context, would mean that the *res judicata* would have binding effects to all shareholders and not only the formal parties in the judicial proceeding.

<sup>6</sup> The authors acknowledge and appreciate the review and comments made on this section by Karine Maillard (Conseillère économique, Ministère de l'Économie et des Finances de France).

<sup>7</sup> See Bollée, Les effets des sentences arbitrales a l'égard des tiers, *Revue de l'Arbitrage* 3 (2015), p. 695.

<sup>8</sup> See Seraglini, Les effets de la sentence, *Revue de l'Arbitrage* 3 (2013), p. 710.

<sup>9</sup> For more details, see, for example: Derains/Descombes, Class actions and arbitration in the European Union – France, in: Billiet (ed), *Class Arbitration in the European Union* (2013), p. 29 and, more recently, Branellec/Lee, Faut-il introduire en France une class action d'actionnaires (Securities Class Actions) ?, *Management & Sciences Sociales, Kedge Business School, Risque: débattre et surtout décider*, 24 (2018), p.19.

<sup>10</sup> The authors acknowledge and appreciate the review and comments made on this section by Peter Sester (Professor of FGV Law School Rio and Vice-President of CAM-CCBC).

<sup>11</sup> For more details, see, for example: Sester, Desafios da arbitragem societária: do efeito erga omnes (extra partes) até a arbitragem coletiva, *Revista de Arbitragem e Mediação* 62 (2019), p. 33. See also Schütze, *Schiedsgericht und Schiedsverfahren* (6<sup>nd</sup> ed. 2016), p. 74.

<sup>12</sup> On the so-called Kapitalanleger-Musterverfahren, see, for example: Rosenberg/Schwab/Gottwald, *Zivilprozessrecht* (18<sup>nd</sup> ed. 2018), p. 260, and Cabral, O novo Procedimento-Modelo (Musterverfahren) alemão: uma alternativa às ações coletivas, *Revista de Processo* 147 (2007), p. 40.

<sup>13</sup> For more details, see, for example: Borris, The European Experience - Germany and the DIS Supplementary Rules for Corporate Law Disputes (DIS-SRCoLD), in: Hanotiau/Schwartz (eds), *Class and Group Actions in Arbitration* (2016), p. 80, Hertel/Covi, Arbitrability of Shareholder Disputes in Germany, *Kluwer Arbitration Blog*, February 7 (2018), and Sester, Desafios da arbitragem societária: do efeito erga omnes (extra partes) até a arbitragem coletiva, *Revista de Arbitragem e Mediação* 62 (2019), p. 32.

<sup>14</sup> Art. 4.1 states that “if Concerned Others join the arbitration as a party within the time limit provided for in Article 3 or Article 9.4 of these DIS-CDR, they shall become a party to the arbitration with all rights and duties pertaining thereto as of the date on which their declaration of joinder is filed with the DIS. If they join as an Intervenor, they shall be entitled to the rights of a compulsory Intervenor as provided for in Section 69 of the German Code of Civil Procedure. Upon their joinder, Concerned Others are entitled to designate additional Concerned Others. Article 3.2 of these DIS-CDR shall apply, mutatis mutandis, with regard to any such additional designated Concerned Others”. But, now under art. 4.2, “if a designated Concerned Other does not join the arbitration within the provided time limit, such Concerned Others shall be deemed to have waived participation in the arbitration, without prejudice to the right to join the arbitration at a later point in time pursuant to Article 4.3 of these DIS-CDR”.

<sup>15</sup> “Unless Concerned Others have expressly waived in writing their right thereto, the arbitral tribunal shall inform, pursuant to Article 4.4 of the Rules, the designated Concerned Others who have not joined the arbitration of the progress of the arbitration by transmitting to the provided addresses of the Concerned Others copies of all Submissions of the parties or of Intervenors as well as any decisions and procedural orders of the arbitral tribunal. This shall apply to other communications from the arbitral tribunal to the parties or Intervenors only insofar as it may be reasonably assumed that such communications are relevant to a subsequent decision of any Concerned Others to join the arbitration. If the DIS transmits decisions by the arbitral tribunal to the parties, the DIS instead of the arbitral tribunal shall transmit such decisions to any designated Concerned Others who have not joined the arbitration”.

<sup>16</sup> “Where multiple arbitrations concerning the same subject matter have been initiated that require a uniform decision applying to all parties and Concerned Others, Articles 9.2 to 9.4 of these DIS-CDR shall apply”

<sup>17</sup> “Article 44 of the Rules shall also apply to all designated Concerned Others.”

<sup>18</sup> “Concerned Others who have not joined the arbitration as a party or as an Intervenor are not entitled to reimbursement of costs”

<sup>19</sup> SHERBY, Eric S. Arbitration in 50 jurisdictions worldwide 2010. WEGEN, Gerhard. WILSKE, Stephan (Ed.). Global Arbitration Review. Access at: <https://www.sherby.co.il/pdf/Israel.pdf>, SASSON, Orna. TAMIR, Doron. Israel. The International Comparative Legal Guide to: International Arbitration 2005. Global Legal Group. Access at: [https://www.arnon.co.il/sites/default/files/files\\_from\\_old/24.%20The%20Israeli%20chapter%20on%20Arbitration.pdf](https://www.arnon.co.il/sites/default/files/files_from_old/24.%20The%20Israeli%20chapter%20on%20Arbitration.pdf) and BAR-NATHAN, Zvi. KAPELIUK, Daphna. International Arbitration 2019: Israel. Access at: <https://practiceguides.chambers.com/practice-guides/comparison/422/3140/6009-6014-6017-6022-6028-6036-6040-6045-6049-6051-6055-6059-6063>

<sup>20</sup> Eric Sherby expressly states that “disputes between shareholders are generally arbitrable, as are disputes between shareholders and the corporation” (SHERBY, Eric S. Arbitration in 50 jurisdictions worldwide 2010. WEGEN, Gerhard. WILSKE, Stephan (Ed.). Global Arbitration Review. Access at: <https://www.sherby.co.il/pdf/Israel.pdf>).

<sup>21</sup> SPRINZAK, Ran. WEISSMAN, Tomer. BEKEL, Hadas. EHRLICH, Naama. Israel. Class Actions: 2020. POLKES, Jonathan. LENDER, David (ed.). Access at: <https://www.lexisnexis.com/uk/lexispsl/disputeresolution/document/393750/5XTB-FHC3-GXFD-824Y>

<sup>22</sup> The same authors also explain, based on judicial decisions, that “a foreign arbitration clause in an agreement will not preclude the filing of a class action” (SPRINZAK, Ran. WEISSMAN, Tomer. BEKEL, Hadas. EHRLICH, Naama. Israel. Class Actions: 2020. POLKES, Jonathan. LENDER, David (ed.). Access at: <https://www.lexisnexis.com/uk/lexispsl/disputeresolution/document/393750/5XTB-FHC3-GXFD-824Y>).



In the same same. Zvi Bar-Nathan and Daphna Kapeliuk state that “the Arbitration Law does not make any reference to class-action arbitrations and these do not take place in Israel” (BAR-NATHAN, Zvi. KAPELIUK, Daphna. International Arbitration 2019: Israel. Access at:

<https://practiceguides.chambers.com/practice-guides/comparison/422/3140/6009-6014-6017-6022-6028-6036-6040-6045-6049-6051-6055-6059-6063>)

<sup>23</sup> Amichai Magen and Peretz Segal explain that “the amendment to the Securities Law proved to be the first in a series of legislative acts incorporating class action provisions modelled after Rule 23 of the U.S. Federal Rules of Civil Procedure – complete with opt-out provisions and certification requirements – into sector-specific Israeli law”. MAGEN, Amichai. SEGAL, Peretz. THE GLOBALIZATION OF CLASS ACTIONSNATIONAL REPORT: ISRAEL. Access at:

[http://globalclassactions.stanford.edu/sites/default/files/documents/Israel\\_National\\_Report.pdf](http://globalclassactions.stanford.edu/sites/default/files/documents/Israel_National_Report.pdf).

<sup>24</sup> MAGEN, Amichai. SEGAL, Peretz. THE GLOBALIZATION OF CLASS ACTIONSNATIONAL REPORT: ISRAEL. Access at:

[http://globalclassactions.stanford.edu/sites/default/files/documents/Israel\\_National\\_Report.pdf](http://globalclassactions.stanford.edu/sites/default/files/documents/Israel_National_Report.pdf).

<sup>25</sup> SHACHAR, Amir. Shareholder activist strategies in Israel. Access at:

<https://www.lexology.com/library/detail.aspx?g=3fa189ab-9f52-4951-9ba0-3355f8f2760e>

<sup>26</sup> “As set forth in s. 3(b)(1) of the Class Actions Law 2006, a person is allowed to commence a class action if he/she has a cause of action that involves essential questions of fact or trial that are shared by all the members listed. The claimant needs to fill a request for approval to the court, which will be granted if the court finds that (i) the case involves questions of fact and law that are common to the whole group, (ii) there is a reasonable possibility that the future decision benefits the group, (iii) the class action is the most suitable legal action for the case, (iv) the claimant is an adequate representative for the group and, finally, (v) the claimant is acting in good faith (s. 8(a)) . In approving the request, the court will define the group in whose name the class action will be managed (s. 10(a) and s. 14(a)). No additional claimants can be included in the group after the date on which the class action was approved” (ROZENT, Gal. ASHLAGI, Hagai. KARMI, Ran. Class/collective actions in Israel: overview. SHAH, Omar (ed.). Class Actions Global Guide. Access at: <https://uk.practicallaw.thomsonreuters.com>).

<sup>27</sup> SPRINZAK, Ran. WEISSMAN, Tomer. BEKEL, Hadas. EHRLICH, Naama. Israel. Class Actions: 2020. POLKES, Jonathan. LENDER, David (ed.). Access at:

<https://www.lexisnexis.com/uk/lexispsl/disputeresolution/document/393750/5XTB-FHC3-GXFD-824Y> and ROZENT, Gal. ASHLAGI, Hagai. KARMI, Ran. Class/collective actions in Israel: overview. SHAH, Omar (ed.). Class Actions Global Guide. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>28</sup> ROZENT, Gal. ASHLAGI, Hagai. KARMI, Ran. Class/collective actions in Israel: overview. SHAH, Omar (ed.). Class Actions Global Guide. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>29</sup> ROZENT, Gal. ASHLAGI, Hagai. KARMI, Ran. Class/collective actions in Israel: overview. SHAH, Omar (ed.). Class Actions Global Guide. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>30</sup> ROZENT, Gal. ASHLAGI, Hagai. KARMI, Ran. Class/collective actions in Israel: overview. SHAH, Omar (ed.). Class Actions Global Guide. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>31</sup> OECD. Minority Protection: Related Party Transactions. Chapter on Israel. Accessed at:

<http://www.oecd.org/corporate/ca/corporategovernanceprinciples/49264021.pdf> and SHACHAR, Amir. Shareholder activist strategies in Israel. Access at: <https://www.lexology.com/library/detail.aspx?g=3fa189ab-9f52-4951-9ba0-3355f8f2760e>

<sup>32</sup> <http://www.isa.gov.il/sites/ISAEng/Departments/Pages/Class-Actions.aspx>

<sup>33</sup> SPRINZAK, Ran. WEISSMAN, Tomer. BEKEL, Hadas. EHRLICH, Naama. Israel. Class Actions: 2020. POLKES, Jonathan. LENDER, David (ed.). Access at: <https://www.lexisnexis.com/uk/lexispsl/disputeresolution/document/393750/5XTB-FHC3-GXFD-824Y>

<sup>34</sup> SPRINZAK, Ran. WEISSMAN, Tomer. BEKEL, Hadas. EHRLICH, Naama. Israel. Class Actions: 2020. POLKES, Jonathan. LENDER, David (ed.). Access at: <https://www.lexisnexis.com/uk/lexispsl/disputeresolution/document/393750/5XTB-FHC3-GXFD-824Y>

<sup>35</sup> The authors acknowledge and appreciate the review and comments made on this section by Carmine Di Noia (Commissioner of CONSOB – Commissione Nazionale per le Società e la Borsa).

<sup>36</sup> See, for example: *Bonato*, Arbitragem societária italiana: análise comparativa sobre a abrangência subjetiva da cláusula compromissória e a nomeação dos árbitros, *Revista de Mediação e Arbitragem* 46 (2015), p. 337. On the arbitrability of class disputes in general, see *Reguizzi/Dragoni*, Class actions and arbitration procedures – Italy, in: Billiet (ed), *Class arbitration in the European Union* (2013), p. 133,

<sup>37</sup> According to art. 105 (intervento volontario), Code of Civil Procedure

<sup>38</sup> According to art. 106 (Intervento su istanza di parte) and art. 107 (Intervento per ordine del giudice), Code of Civil Procedure

<sup>39</sup> See, for example: *Gradi*, L'intervento volontario e la chiamata in causa dei terzi nel processo arbitrale, *Rivista dell'arbitrato* 2 (2010), p. 283.

<sup>40</sup> The authors acknowledge and appreciate the review and comments made on this section by Laura Leal (Coordinator of Regulatory Policy and International Affairs Department, at the CMVM – Comissão do Mercado de Valores Mobiliários | Portuguese Securities Market Commission) and Professor Dario Moura Vicente (President of APA and Full Professor at Faculdade de Direito da Universidade de Lisboa). Professor Dario Moura Vicente gave us very helpful information about the bill drafted by the *Secretaria de Estado da Justiça* and also about the bill drafted by the *Associação Portuguesa de Arbitragem – APA*.

<sup>41</sup> Standing for the arbitrability: BARROCAS, Manuel Pereira. *Manual de arbitragem*. 2. ed. Coimbra: Almedina, 2013, p. 117, and CORDEIRO, Antonio Menezes. *Tratado da arbitragem*. Coimbra: Almedina, 2015, p. 101. Against: CAMELO, Antonio Sampaio. *Arbitragem de litígios societários*. Temas de direito da arbitragem. Coimbra: Coimbra, 2013, p. 343.

<sup>42</sup> Accessed at: <https://a.storyblok.com/f/46533/x/644d9d61e0/discussao-anteprojeto-diploma-legislativo-regras-arb-materia-societaria.pdf>

<sup>43</sup> Accessed at: <https://a.storyblok.com/f/46533/x/96f24127f1/discussao-anteprojeto-regulamento-arb-societaria-p-centros-arb.pdf>

<sup>44</sup> The authors acknowledge and appreciate the review and comments made on this section by Jonathan Lim (Counsel at WilmerHale, in London), in particular essential explanations about the *Tomolugen v. Silica* case, the representative actions in the Singaporean Law and the *Raffles Town Club* case.

<sup>45</sup> [2015] SGCA 57.

<sup>46</sup> First, the Court explained that in its view “a dispute over the liquidation of an insolvent company is non-arbitrable because such a liquidation is a process in which the greater public beyond the parties to the dispute have an interest”. Then, the judgment made clear that “there is certainly nothing in the text of s.

216 [which deals with unfair prejudice] to suggest an express or implied preclusion of arbitration”, and that “there is, in general, no public element in disputes of this nature which mandate the conclusion that it would be contrary to public policy for them to be determined by an arbitral tribunal rather than by a court”. Finally, the Court stated that “the fact that the relief sought might be beyond the power of the tribunal to grant does not in and of itself make the subject matter of the dispute non-arbitrable”. In sum, the court distinguished a case concerning the liquidation of an insolvent company from a case concerning a minority oppression dispute (para 84). In a minority oppression action, one of the remedies available is the winding up of the company, but despite the fact that the arbitral tribunal cannot grant such an order (paras 98 – 103), and the procedural complexity of having to send the dispute to the court to obtain the remedy of winding up (para 105), the court found that minority oppression actions can be arbitrated. Following this precedent, the courts repeated the same approach in *Gulf v. Rex International* ([2017] SGHC 210) and *BTY v BUA* [2018] SGHC 213.

<sup>47</sup> YEAP, Andre. POON, Kelvin. PANG, Alessa. *International Arbitration 2019: Singapore*. Access at: <https://practiceguides.chambers.com/practice-guides/international-arbitration-2019/singapore> and ROBERTS, Ian. KILNER, Vanessa. *Representative action in Singapore: The decision in Koh Chong Chiah v Treasure Resort*. Access at: <https://www.clydeco.com/insight/article/representative-action-in-singapore-the-decision-in-koh-chong-chiah-v-treasu>.

<sup>48</sup> CHIA, Daniel. WONG, Jeanette. *Class/collective actions in Singapore: overview*. SHAH, Omar (ed.). *Class Actions Global Guide*. Access at: <https://uk.practicallaw.thomsonreuters.com>, and Global Class Actions Exchange. Access at: [http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore\\_National\\_Report.pdf](http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore_National_Report.pdf)

<sup>49</sup> ROBERTS, Ian. KILNER, Vanessa. *Representative action in Singapore: The decision in Koh Chong Chiah v Treasure Resort*. Access at: <https://www.clydeco.com/insight/article/representative-action-in-singapore-the-decision-in-koh-chong-chiah-v-treasu>, and Global Class Actions Exchange. Access at: [http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore\\_National\\_Report.pdf](http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore_National_Report.pdf)

<sup>50</sup> See para 57; Holding (4). *Koh Chong Chiah v Treasure Resort Pte Ltd* [2013] 4 SLR 1204 and ROBERTS, Ian. KILNER, Vanessa. *Representative action in Singapore: The decision in Koh Chong Chiah v Treasure Resort*. Access at: <https://www.clydeco.com/insight/article/representative-action-in-singapore-the-decision-in-koh-chong-chiah-v-treasu>

<sup>51</sup> CHIA, Daniel. WONG, Jeanette. *Class/collective actions in Singapore: overview*. SHAH, Omar (ed.). *Class Actions Global Guide*. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>52</sup> Global Class Actions Exchange. Access at: [http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore\\_National\\_Report.pdf](http://globalclassactions.stanford.edu/sites/default/files/documents/Singapore_National_Report.pdf)

<sup>53</sup> Both were related to disputes between club members and club managers. See: CHIA, Daniel. WONG, Jeanette. *Class/collective actions in Singapore: overview*. SHAH, Omar (ed.). *Class Actions Global Guide*. Access at: <https://uk.practicallaw.thomsonreuters.com>.

<sup>54</sup> QUAH, Michelle. *Are class actions good for investors and Singapore markets?* Access at: <https://www.asiaone.com/are-class-actions-good-investors-and-singapore-markets>

<sup>55</sup> The authors acknowledge and appreciate the review and comments made on this section by Mélanie Riofrio (Secretary-General of the Centro de Arbitraje Internacional de Madrid – CIAM), Fernando Alvarez-Cienfuegos Rico (Spanish Ministry of Economy / Ministerio de Economía y Empresa de España) and Peter Barna (Counsel at Madrid Court of Arbitration).

<sup>56</sup> Since it refers expressly to *sociedades de capital* and publicly held companies are defined as *sociedades de capital* by art. 1 of the *Ley de Sociedades de Capital*.

<sup>57</sup> See, for example *Tarrío Berjano*, 'Ley de Arbitraje, Artículo 11 bis [Arbitraje estatutario]', in: *González-Bueno* (ed), *Comentarios a la Ley de Arbitraje* (2014) p. 275 and *González-Bueno*, 'Spanish Arbitration Act, Article 11bis [Corporate arbitration]', in: *González-Bueno* (ed), *The Spanish Arbitration Act: A Commentary*(2016), p 71, and *Perales Viscasillas*, *La reforma de la ley de arbitraje, Arbitraje IV(3)* (2011), p. 678.

<sup>58</sup> CORREA, Laura Lozano Correa. Spanish Arbitration Act, Article 37. *The Spanish Arbitration Act: A Commentary*. GONZÁLEZ-BUENO, Carlos (ed). Dykinson: S.L., 2016, p. 229.

<sup>59</sup> See, for example, art. 46 (3) of the CIMA Rules: "The Arbitral Tribunal shall quantify and apportion with reasons the costs of arbitration, based, firstly, on the agreement of the parties. In absence thereof, the Arbitral Tribunal will consider the success or failure of the respective claims and defenses, the degree of cooperation between the parties during the arbitration and any other circumstances that the Arbitral Tribunal deems appropriate".

<sup>60</sup> For more information (as of December 2019), see, for example: <https://gettingthedealthrough.com/area/94/jurisdiction/21/litigation-funding-spain/>.

<sup>61</sup> "TFP in Spain has been practised for some years, mainly in the field of competition law and other mass litigation, insolvency and also investment arbitration. While no Spanish investment fund seems to exist to date, a few companies (mainly internet platforms dealings with internal small claims) propose no-win-no-fee arrangements to process and enforce scalable small claims. The legal perspective for TPF in the Spanish legal market has recently been discussed, concluding that, in the light of the current legal framework, no specific prohibition would apply. As to the nature of the contract and the related applicable regulatory regime, it has been excluded that a TPF contract could be a loan or an assignment of claims but rather, following the prevailing opinion among German scholars, a silent partnership" (*Solas*, *Third Party Funding: law, economics and policy* (2019), p. 114)

<sup>62</sup> BETANCOR, Armando. CERVERA, César. BAYO, Carolina. CABRERA, Francisco. FRUTOS, Eduardo. *Spain. Litigation Funding 2020*. FRIEL, Steven. BARNES, Jonathan (Ed). *Law Business Research*: London, 2019, accessed at: <https://woodsfordlitigationfunding.com/wp-content/uploads/2020/01/GTDT2020-Spain.pdf>.

<sup>63</sup> BETANCOR, Armando. CERVERA, César. BAYO, Carolina. CABRERA, Francisco. FRUTOS, Eduardo. *Spain. Litigation Funding 2020*. FRIEL, Steven. BARNES, Jonathan (Ed). *Law Business Research*: London, 2019, accessed at: <https://woodsfordlitigationfunding.com/wp-content/uploads/2020/01/GTDT2020-Spain.pdf>.

<sup>64</sup> BETANCOR, Armando. CERVERA, César. BAYO, Carolina. CABRERA, Francisco. FRUTOS, Eduardo. *Spain. Litigation Funding 2020*. FRIEL, Steven. BARNES, Jonathan (Ed). *Law Business Research*: London, 2019, accessed at: <https://woodsfordlitigationfunding.com/wp-content/uploads/2020/01/GTDT2020-Spain.pdf>.

<sup>65</sup> *González-Bueno*, Spanish Arbitration Act, Article 11bis (corporate arbitration), in: *González-Bueno*(ed), *The Spanish Arbitration Act: A commentary* (2016), p. 74.

<sup>66</sup> In her speech at the IV Oxford Symposium on Comparative International Commercial Arbitration, Sophie Lamb QC explained that disputes involving internal company matters are contractual in nature and, therefore, can be adjudicated through arbitration. She also stated that there is no specific legal prohibition

to arbitrate them. In theory, hence, shareholders' disputes are arbitrable in England and Wales (LAMB, Sophie. Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford).

<sup>67</sup> Fulham Football Club (1987) Ltd v Richards & Anor [2011] EWCA Civ 855 (21 July 2011).

<sup>68</sup> Lord Justice Patten made clear that "the only restriction placed upon the arbitrator is in respect of the kind of relief which can be granted".

<sup>69</sup> Lord Justice Longmore made clear that "it is well settled that the fact that an arbitrator cannot give all the remedies which a court could does not afford any reason for treating an arbitration agreement as of no effect" as well as "the inability to give a particular remedy is just an incident of the agreement which the parties have made as to the method by which their disputes are to be resolved".

<sup>70</sup> See, for example: Foss v Harbottle (1843), Mozley v Alston (1847), Hawkesbury v Landmark (1969) and Prudential v Newman (1982). See also: FRENCH, Derek. Mayson, French and Ryan on Company Law. 34 ed. Oxford: OUP, 2017, p. 554.

<sup>71</sup> There are three types of derivative claims in English Law. The first type is set forth in Part 11 of the Companies Act 2006 and may be brought against a director who caused damages to the company for negligence, default, breach of duty or breach of trust (s. 260(3) of the Companies Act 2006). The second type is the relief which the court can grant in relation to unfair prejudice petition presented under s. 994 of the Companies Act 2006. In this case, the derivative claim can be brought in negligence against a third party irrespective of whether there was also a breach of duty by one of the company's directors. The third and last one is a common law multiple derivative claim in respect of overseas companies in cases of fraud on minorities (negligence is not an enough ground for this type). In this report, we refer only to the first type.

<sup>72</sup> According to Andrew Dickinson, in his report to the British Institute of International and Comparative Law, "any judgment on a derivative claim binds the company as if it had brought the action" (DICKINSON, Andrew. The Effect in the European Community of Judgments in Civil and Commercial Matters: Recognition, Res Judicata and Abuse of Process. British Institute of International and Comparative Law. Accessed at: [https://www.biiicl.org/files/3480\\_england\\_&\\_wales\\_final\\_c.pdf](https://www.biiicl.org/files/3480_england_&_wales_final_c.pdf). The author mentions the following case in support of his conclusion: Beattie v Beattie Ltd [1938] Ch 708, at 708).

<sup>73</sup> In this sense: LAMB, Sophie. Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford.

<sup>74</sup> LAMB, Sophie. Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford.

<sup>75</sup> LAMB, Sophie. Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford.

<sup>76</sup> ZUCKERMAN, Adrian. Zuckerman on Civil Procedure. 3rd ed. London: Sweet & Maxwell, 2013, p. 664, HUNTER, Ian. Flannery, Louis. Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 197 and LAMB, Sophie. Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford.

<sup>77</sup> Access at: <https://www.ashurst.com/en/news-and-insights/legal-updates/quickguide-collective-actions--uk-guide/>

<sup>78</sup> ZUCKERMAN, Adrian. *Zuckerman on Civil Procedure*. 3rd ed. London: Sweet & Maxwell, 2013, p. 677.

<sup>79</sup> SMITH, Vincent. YALABIK, Fulya Teomete. *Focus on Collective Redress: England and Wales*. British Institute of International and Comparative Law. Accessed at: <https://www.collectiveredress.org/collective-redress/reports/ew/generalcollectiveredressmechanisms>

<sup>80</sup> Ian Hunter and Louis Flannery explain that “there is no equivalent mechanism available in English arbitrations” HUNTER, Ian. Flannery, Louis. *Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union*. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 210-211).

<sup>81</sup> BILLIET, Philippe. *Collective Redress and Class Arbitration in the EU. Class and Group Actions in Arbitration*. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). *Dossiers of the ICC Institute of World Business Law*. The Hague: Kluwer, v. 14, 2016, p. 66 and HUNTER, Ian. Flannery, Louis. *Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union*. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 198.

<sup>82</sup> HUNTER, Ian. Flannery, Louis. *Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union*. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 204 and BILLIET, Philippe. *Collective Redress and Class Arbitration in the EU. Class and Group Actions in Arbitration*. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). *Dossiers of the ICC Institute of World Business Law*. The Hague: Kluwer, v. 14, 2016, p. 66.

<sup>83</sup> LAMB, Sophie. *Panel on class arbitration in investor-company disputes. IV Oxford Symposium on Comparative International Commercial Arbitration. 15th November 2019. University of Oxford and HUNTER, Ian. Flannery, Louis. Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union*. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 201-202.

<sup>84</sup> The authors acknowledge and appreciate the review and comments made on this section by Guilherme Recena Costa (Associate at Debevoise & Plimpton – New York).

<sup>85</sup> <https://www.federalrulesofcivilprocedure.org/frcp/title-iv-parties/rule-23-class-actions/>

<sup>86</sup> KENT, Rachael. STRING, Marik. *Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges*. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 857-858 and NETTLETON, Stacy. HOCHSTADT, Eric. SINGH, David. OBARO, Bambo. BARRINGTON, Luna. CONNORS, Matthew. *United States. Class Actions 2020*. 5th ed. POLKES, Jonathan. LENDER, David (ed.). Law Business Research Ltd 2019.

<sup>87</sup> NETTLETON, Stacy. HOCHSTADT, Eric. SINGH, David. OBARO, Bambo. BARRINGTON, Luna. CONNORS, Matthew. *United States. Class Actions 2020*. 5th ed. POLKES, Jonathan. LENDER, David (ed.). Law Business Research Ltd 2019.

<sup>88</sup> Ibidem. Ibidem.

<sup>89</sup> After the filing and as soon as practically possible, the court must determine whether the lawsuit is going to proceed as a class action or as an individual claim. Rule 23(a) establishes four requirements for a legal action to be accepted as a class action: numerosity (a high number of possible class members), commonality (questions of law or fact common among the class members), typicality (the claims/defences presented by the claimant are typical of the class) and adequacy (the claimant is an adequate representative party) . The claimant has the burden to show, by a preponderance of the evidence (mere

allegations will not suffice), that all four requirements are met. Defendants are allowed to present their arguments at this stage of the proceedings in order to persuade the court to deny the certification. The court may hold a hearing on the issues to hear the parties and make a decision. If the claimant shows that the legal action satisfies the four requirements, the court will issue a certification order (i) defining the class (and the issues, claims and defences involved), (ii) appointing the class counsel and (iii) directing appropriate notice to the members of the represented class (Rule 23(c)(1)). Appellate proceedings are available, whether the court granted or denied the class action certification (Rule 23(f)). The notice sent to the class members is of particular importance (Rule 23(c)(2)). It must contain detailed information about the case and must let the individual members know that they have the right to opt-out of the class action; otherwise they will be bound by the decision. According to Rule 23(e)(1), settlements must be approved by the court, which will take reasonable steps to notify the class members of the proposal. Members can file a written objection to the settlement with the court. In some cases, state and federal regulators must also be notified of the settlement. The Rules also require the court to hold a hearing to check if the settlement is the product of an arm's length negotiation and if its terms are "fair, reasonable, and adequate" (Rule 23(e)(2)). As set forth in Rule 23(e)(4), if any member disagrees with the proposed terms, he/she can opt-out of the settlement and pursue their claims individually. The decision on the merits binds all class members (except those who have previously opted-out) and prevents them from filing their own claims individual . Appellate proceedings are available, as in all court proceedings.

<sup>90</sup> Class arbitration refers to the application of principles of class action suits in the arbitration context and allows for a group of claimants to advance their claims collectively in one action against a single or group of respondents (ORTA, David M. LEE, Matthew A. Lee. ROWE, Brian. Class Action Arbitration under U.S. Jurisprudence. International Arbitration in the United States. CHENG, Tai-Heng. LA CHUISA, Jenelle E. SCHANER, Lawrence. SHORE, Laurence. SENN, Mara V.J. TAN, Liang-Ying (eds.). The Hague: Kluwer, 2017, p. 651).

<sup>91</sup> DRAHOZAL, Christopher R. Class Arbitration in the United States. Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 13. According to Gary B. Born and Claudio Salas, "over the past two decades, the use of class action procedures migrated from litigation to arbitration in domestic U.S. practice" as well as "state courts, notably in California, paved the way in permitting arbitrations to be conducted on a class basis, on behalf of large numbers of similarly-situated claimants (usually consumers), all having identical arbitration agreements with the same defendant" (BORN, Gary. SALA, Claudio. The U.S. Supreme Court and Class Arbitration: A Tragedy of Errors. Access at: <http://arbitrationblog.kluwerarbitration.com/2011/07/01/the-u-s-supreme-court-and-class-arbitration-a-tragedy-of-errors/>. On 01.07.2011).

<sup>92</sup> Green Tree Financial Corp. v. Bazzle, 539 U.S. 444 (2003)

<sup>93</sup> HUNTER, Ian. Flannery, Louis. Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 193.

<sup>94</sup> KENT, Rachael. STRING, Marik. Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 857-858.

<sup>95</sup> DRAHOZAL, Christopher R. Class Arbitration in the United States. Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 24.

<sup>96</sup> In fact, state courts decided to invalidate all these waiver clauses, applying the so-called *Discover Bank* rule (California Supreme Court – *Discover Bank v. Superior Court of Los Angeles* (36 Cal. 4th 148, 163-164 (2005))).

<sup>97</sup> *Stolt-Nielsen S. A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010).

<sup>98</sup> KENT, Rachael. STRING, Marik. Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 860.

<sup>99</sup> *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011).

<sup>100</sup> In other words, the Court understood that states cannot pass laws that create specific grounds to challenge the validity of arbitration agreements and therefore authorised the class arbitration waiver clauses

<sup>101</sup> *Am. Express Co. v. Italian Colors Rest.*, 570 U.S. 228 (2013).

<sup>102</sup> *Lamps Plus, Inc. v. Varela*, 587 U.S. \_\_\_\_ (2019).

<sup>103</sup> *Green Tree v Bazzle; Stolt-Nielsen v. AnimalFeeds; AT&T v. Concepcion; American Express v. Italian Colors Oxford Health Plans v. Sutter; DirectTV v Imburgia; and Lamps v. Varela. In the same sense:* ORTA, David M. LEE, Matthew A. Lee. ROWE, Brian. Class Action Arbitration under U.S. Jurisprudence. International Arbitration in the United States. CHENG, Tai-Heng. LA CHUISA, Jenelle E. SCHANER, Lawrence. SHORE, Laurence. SENN, Mara V.J. TAN, Liang-Ying (eds.). The Hague: Kluwer, 2017, p. 645 and KENT, Rachael. STRING, Marik. Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 872.

<sup>104</sup> *American Express v. Italian Colors; Lamps v. Varela. In the same sense:* DRAHOZAL, Christopher R. Class Arbitration in the United States. Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 13.

<sup>105</sup> *Stolt-Nielsen v. AnimalFeed; and Lamps v. Varela. In the same sense:* KENT, Rachael. STRING, Marik. Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 872.

<sup>106</sup> *Stolt-Nielsen v. AnimalFeed; and Lamps v. Varela. In the same sense:* LEE, Matthew. BENTO, Lucas. Class Arbitration In The United States Survives Another Battle, But Will It Survive The War? Access at: <http://arbitrationblog.kluwerarbitration.com/2013/06/21/class-arbitration-in-the-united-states-survives-another-battle-but-will-it-survive-the-war/>. On 21.06.2013.

<sup>107</sup> *AT&T v. Concepcion; American Express v. Italian Colors; and DirectTV v Imburgia. In the same sense:* KENT, Rachael. STRING, Marik. Availability of Class Arbitration Under US Law. Legitimacy: Myths, Realities, Challenges. BERG, Albert Jan Van den (ed). The Hague: Kluwer, ICCA Congress Series, v. 18, 2015, p. 872 and 873.

<sup>108</sup> *Oxford Health Plans v. Sutter. In the same sense:* ORTA, David M. LEE, Matthew A. ROWE, Brian. Class Action Arbitration under U.S. Jurisprudence. International Arbitration in the United States. CHENG, Tai-Heng. LA CHUISA, Jenelle E. SCHANER, Lawrence. SHORE, Laurence. SENN, Mara V.J. TAN, Liang-Ying (eds.). The Hague: Kluwer, 2017, p. 653.



<sup>109</sup> ORTA, David M. LEE, Matthew A. ROWE, Brian. Class Action Arbitration under U.S. Jurisprudence. International Arbitration in the United States. CHENG, Tai-Heng. LA CHUISA, Jenelle E. SCHANER, Lawrence. SHORE, Laurence. SENN, Mara V.J. TAN, Liang-Ying (eds.). The Hague: Kluwer, 2017, p. 654.

<sup>110</sup> In 2015, the Consumer Financial Protection Bureau (CFPB) issued proposals, on the basis of its earlier CFPB Study, for rules to regulate use of arbitration in consumer financial transactions: [https://files.consumerfinance.gov/f/201510\\_cfpb\\_small-business-review-panel-packet-explaining-the-proposal-under-consideration.pdf](https://files.consumerfinance.gov/f/201510_cfpb_small-business-review-panel-packet-explaining-the-proposal-under-consideration.pdf). The Financial Industry Regulatory Authority (FINRA), the Securities Exchange Commission (SEC) and the National Association of Securities Dealers (NASD) have also taken action reflecting policy preferences for class arbitration over numerous individual arbitrations to resolve multiple or similar disputes.

<sup>111</sup> In the case of JAMS, their rules expressly state that “JAMS will not administer a demand for class action arbitration when the underlying agreement contains a class preclusion clause, or its equivalent, unless a court orders the matter or claim to arbitration as a class action” (Rule 1(a)).

<sup>112</sup> According to James Carter, “by 2009, the AAA cases had resulted in 48 Class Determination Awards, each of which was automatically stayed for a second time so that any party could go to court to ask for confirmation or vacatur”. Then, the author informs that “exactly half of those awards granted class arbitration status” (CARTE, James H. Class arbitration in the United States: life after death? Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 14).

<sup>113</sup> In the case of JAMS, Rule 2 (construction of the arbitration clause) states that “subject to Rule 1(a), once appointed, the Arbitrator, following the law applicable to the validity of the arbitration clause as a whole, or the validity of any of its terms, or any court order applicable to the matter, shall determine as a threshold matter whether the arbitration can proceed on behalf of or against a class”.

<sup>114</sup> HUNTER, Ian. Flannery, Louis. Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 193.

<sup>115</sup> HUNTER, Ian. Flannery, Louis. Class action and arbitration procedures – United Kingdom. Class arbitration in the European Union. BILLIET, Philippe (ed.). Antwerpen: Maklu, 2013, p. 193.

<sup>116</sup> Rule 3. Prerequisites to a Class Certification. (a) The Arbitrator shall determine whether a class should be certified. In making that determination, the Arbitrator shall consider the criteria enumerated in this Rule 3 and any law that the Arbitrator determines applies to the arbitration. The Arbitrator also shall determine whether one or more members of a class may act in the arbitration as representative parties on behalf of all members of the class described. The Arbitrator shall permit a class member to serve as a representative only if the conditions set forth in the Federal Rules of Civil Procedure, Rule 23(a), are met.

<sup>117</sup> “The best notice practicable under the circumstances”.

<sup>118</sup> JAMS Rules also provide for the notice of class determination (Rule 4).

<sup>119</sup> AAA Supplementary Rules for Class Arbitrations. Rule 6. Notice of Class Determination. (...). (b) The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class judgment on class members.

<sup>120</sup> JAMS Class Action Procedures. Rule 4. Notice of Class Determination. (...). The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class award on class members.

<sup>121</sup> CARTE, James H. Class arbitration in the United States: life after death? Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 13.

<sup>122</sup> James Carter informs that “by 2009, no AAA class arbitration had yet resulted in a merits award” (CARTE, James H. Class arbitration in the United States: life after death? Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 14).

<sup>123</sup> DRAHOZAL, Christopher R. Class Arbitration in the United States. Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 27.

<sup>124</sup> Christopher Drahozal, based on data released in 2009, explains that “while most of the claims seeking class arbitration were brought by consumers (106, or 37%) or employees (96, or 34%), a surprising number involved business claimants (81, or 28%), typically small businesses” (DRAHOZAL, Christopher R. Class Arbitration in the United States. Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 13).

<sup>125</sup> BORN, Gary. International Commercial Arbitration. 2<sup>nd</sup> ed. The Hague: Kluwer, 2014, v. 1, p. 1.029.

<sup>126</sup> See February 11, 2019 Public Statement by Chairman Jay Clayton at <https://www.sec.gov/news/public-statement/clayton-statement-mandatory-arbitration-by-law-provisions>

<sup>127</sup> 116 F.Supp.3d 368 (2015).

<sup>128</sup> <https://www.leagle.com/decision/infdco20150731a18%20>

<sup>129</sup> CARTE, James H. Class arbitration in the United States: life after death? Class and Group Actions in Arbitration. HANOTIAU, Bernard. SCHWARTZ, Eric (eds.). Dossiers of the ICC. The Hague: Kluwer, v. 14, 2016, p. 19.

<sup>130</sup> <https://www.finra.org/arbitration-mediation/printable-code-arbitration-procedure-13000#13204>

<sup>131</sup> <https://www.finra.org/arbitration-mediation/printable-code-arbitration-procedure-12000#12204>

<sup>132</sup> Code of Arbitration Procedure for Industry Disputes, s. 13204(a): “Class action claims may not be arbitrated under the Code”. Code of Arbitration Procedure for Customer Disputes, s. 12204(a): “Class action claims may not be arbitrated under the Code”.

<sup>133</sup> OECD (2015), G20/OECD Principles of Corporate Governance, OECD Publishing, Paris, p. 18.

<sup>134</sup> OECD (2013), Supervision and Enforcement in Corporate Governance, Corporate Governance, OECD Publishing, p. 11.

<sup>135</sup> “There is no question that Brazilian existing private enforcement mechanisms need improvements in order to enhance their effectiveness in the field of corporate law and capital markets – specially to address the issue of shareholders’ redress” (Strengthening the enforcement of shareholders’ rights (interim report) (2019), p. 4). For more details, see pp. 11-17.

<sup>136</sup> [http://www.cvm.gov.br/export/sites/cvm/publicacao/boletimmercado/anexos/BoletimdeMercado\\_75\\_01\\_2020.pdf](http://www.cvm.gov.br/export/sites/cvm/publicacao/boletimmercado/anexos/BoletimdeMercado_75_01_2020.pdf)

<sup>137</sup> <https://valorinveste.globo.com/mercados/renda-variavel/bolsas-e-indices/noticia/2019/11/14/numero-de-empresas-na-bolsa-e-o-menor-desde-1996.ghtml>

<sup>138</sup> Cox/Thomas, SEC Enforcement Heuristics: An empirical enquiry, *Duke Law Journal* 53 (2003), p. 737.

<sup>139</sup> This summary of Cox and Thomas study was provided for in OECD (2013), *Supervision and Enforcement in Corporate Governance*, Corporate Governance, OECD Publishing, p. 11.

<sup>140</sup> In line with suggestions made by the working group on [Strengthening the enforcement of shareholders' rights \(interim report\)](#) (2019), p. 16.

<sup>141</sup> *Strengthening the enforcement of shareholders' rights (interim report)* (2019), p. 19.

<sup>142</sup> See, for example: *Kohlbach*, *Participação de terceiros na arbitragem* (2020), p. 111, and *Recena Costa*, *Partes e terceiros na arbitragem* (2015), p. 89.

<sup>143</sup> “Adhesion to the special segments is voluntary, but each segment requires the adoption of corporate governance rules beyond those required in the law. Novo Mercado is the segment with the highest standards of corporate governance practices” (*Strengthening the enforcement of shareholders' rights (interim report)* (2019), p. 18). For more details, see: [http://www.bmfbovespa.com.br/pt\\_br/listagem/acoes/segmentos-de-listagem/sobre-segmentos-de-listagem/](http://www.bmfbovespa.com.br/pt_br/listagem/acoes/segmentos-de-listagem/sobre-segmentos-de-listagem/)

<sup>144</sup> The authors acknowledge and appreciate the data provided by Felipe Veras (Legal Coordinator at CAM-B3) on 09.03.2020.

<sup>145</sup> Since 2018, *Câmara de Arbitragem do Mercado* has been publishing extracts of the arbitral awards. In its second edition, the report has already published extracts of more than 30 arbitral awards.

<sup>146</sup> Accessed at: <https://ccbc.org.br/cam-ccbc-centro-arbitragem-mediacao/sobre-cam-ccbc/estatisticas-gerais/>

<sup>147</sup> The authors acknowledge and appreciate the data provided by Eleonora Coelho (President of CAM-CCBC) on 24.03.2020.

<sup>148</sup> The authors acknowledge and appreciate the data provided by João Luiz Lessa Neto (Secretary-General of the Chamber of Conciliation, Mediation and Arbitration of São Paulo – Ciesp/Fiesp) and Lilian Bertolani (Deputy Secretary-General of the Chamber of Conciliation, Mediation and Arbitration of São Paulo – Ciesp/Fiesp) on 25.03.2020.

<sup>149</sup> The authors acknowledge and appreciate the data provided by Augusto Tolentino (President of CAMARB) on 25.03.2020.

<sup>150</sup> The authors acknowledge and appreciate the data provided by Carolina da Rocha Morandi (Secretary-General of the Centre for Arbitration and Mediation AMCHAM) on 31.03.2020.

<sup>151</sup> PARGENDLER, Mariana. PRADO, Viviane Muller. BARBOSA JR., Alberto. Cláusulas arbitrais no mercado de capitais brasileiro: alguns dados empíricos. *Revista de arbitragem e mediação*. São Paulo: RT, v. 40. Accessed at: <http://www.revistadostribunais.com.br>.

<sup>152</sup> See also: *González-Bueno*, Spanish Arbitration Act, Article 11bis (corporate arbitration), in: González-Bueno(ed), *The Spanish Arbitration Act: A commentary* (2016), p. 74.

<sup>153</sup> For more details, see, for example: *Eizirik*, A constitucionalidade do art. 136-A da lei das S.A., *Revista de Arbitragem e Mediação* 58 (2018), p. 131.

<sup>154</sup> STF, SE n. 5.206-7/ES.

<sup>155</sup> Under art. 11.1 of Annex 5 of the DIS Rules, “the effects of an arbitral award extend to those Concerned Others that have been designated as such within the time limits provided in these DIS-CDR, regardless of whether they have availed themselves of the opportunity to join the arbitration as a party or as an Intervenor. The shareholders designated as Concerned Others within the provided time limits agree to recognize the effects of an arbitral award rendered in accordance with these DIS-CDR”.

<sup>156</sup> <http://arbitrationblog.kluwerarbitration.com/2018/02/07/arbitrability-shareholder-disputes-germany/>

<sup>157</sup> See also the conclusions of the working group on Strengthening the enforcement of shareholders’ rights (interim report) (2019), p. 23 and the opinion of scholars *Coelho*, A necessidade da criação de regulamentos adaptados para arbitragens coletivas no mercado de capitais, in: Yarshell/Setoguti, *Processo societário*, vol. 3 (2018), p. 127, e *Sester*, Desafios da arbitragem societária: do efeito erga omnes (extra partes) até a arbitragem coletiva, *Revista de Arbitragem e Mediação* 62 (2019), p. 35.

<sup>158</sup> <https://www.sec.gov/news/speech/jackson-shareholders-conversation-about-mandatory-arbitration-022618>. See also Strengthening the enforcement of shareholders’ rights (interim report) (2019), p. 20.

<sup>159</sup> See, for example: *Wald/Suassuna*, A Corte Suprema norte-americana e a evolução da class arbitration, *Revista de Arbitragem e Mediação* 63 (2019) p. 279.

<sup>160</sup> For more details on the issue under Brazilian law, see, for example: *Franzoni*, Arbitragem societária (2015), p. 73, *Martins*, A arbitrabilidade subjetiva e a imperatividade dos direitos societários como pretensão fator impeditivo para a adoção da arbitragem nas sociedades anônimas, in: Yarshell/Setoguti, *Processo societário*, vol. 1 (2012), p. 46), and *Tellechea*, Arbitragem nas sociedades anônimas: direitos individuais e princípio majoritário (2016), p. 352

<sup>161</sup> See, for example: *Müssnich/Peres*, Arbitrabilidade subjetiva no direito societário e direito de recesso, in: *Melo/Beneduzi*, A reforma da arbitragem (2016), p. 673), *Weber*, Arbitragem e direito societário, in: *Melo/Beneduzi*, A reforma da arbitragem (2016), p. 59, and *Fichtner/Mannheimer/Monteiro*, Teoria geral da arbitragem (2018), p. 353-361.

<sup>162</sup> For more details, see *Tucci*, Impugnação judicial da deliberação de Assembleia societária e projeções da coisa julgada, in: Yarshell/Setoguti, *Processo societário*, vol. 1 (2012), p. 461).

<sup>163</sup> The German BGH does not yet allow the application of these rules to publicly listed companies.

<sup>164</sup> Beschluss des II. Zivilsenats vom 6.4.2009 - II ZR 255/08.

<sup>165</sup> AAA Supplementary Rules for Class Arbitrations. Rule 6. Notice of Class Determination. (...). (b) The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class judgment on class members.

<sup>166</sup> JAMS Class Action Procedures. Rule 4. Notice of Class Determination. (...). The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class award on class members.

<sup>167</sup> See, for example: *Carmona*, Arbitragem e processo (3<sup>rd</sup> ed. 2009), p. 15, and *Fichtner/ Mannheimer/ Monteiro*, Teoria geral da arbitragem (2018), p. 120

<sup>168</sup> See *Aragão*, Aspectos processuais da legislação societária, in: Yarshell/Setoguti, Processo societário, vol. 3 (2018), p. p. 625.

<sup>169</sup> *Am. Express Co. v. Italian Colors Rest.*, 570 U.S. 228 (2013).

<sup>170</sup> See, for example: *Salomão Filho*, Breves notas sobre a transparência e publicidade na arbitragem societária, in: Yarshell/Setoguti, Processo societário, vol. 3 (2018), p. 39. See also *Ferro*, A confidencialidade da arbitragem: o abuso nas exceções, in: Venancio Filho/Lobo/Rosman, Lei das S.A. em seus 40 anos (2016), p. 535.

<sup>171</sup> AAA Supplementary Rules for Class Arbitrations. Rule 6. Notice of Class Determination. (a) In any arbitration administered under these Supplementary Rules, the arbitrator shall, after expiration of the stay following the Class Determination Award, direct that class members be provided the best notice practicable under the circumstances (the “Notice of Class Determination”). The Notice of Class Determination shall be given to all members who can be identified through reasonable effort.

<sup>172</sup> JAMS Class Action Procedures. Rule 4. Notice of Class Determination. The Arbitrator shall direct that class members be provided the best notice practicable under the circumstances (“Notice of Class Determination”). The Notice of Class Determination shall be given to all members who can be identified through reasonable effort.

<sup>173</sup> See, for example: *Zahr Filho*, Conflitos societários multipartes com repercussão coletiva submetidos à clausula compromissória estatutária: intervenção de terceiros e consolidação, in: Yarshell/Setoguti, Processo societário, vol. 2 (2012), p. 717.

<sup>174</sup> Born, International commercial arbitration, vol. 1 (2014), p. 1388.

<sup>175</sup> Although under the DIS Rules 1.4 Annex 5 (Supplementary Rules for Corporate Disputes) is only applicable when the parties have agreed to apply such Annex.

<sup>176</sup> See, for example: *Hazard/Leubsforf/Basset*, Civil procedure (6<sup>st</sup> ed. 2011), p. 647.

<sup>177</sup> See, for example: *Marinoni*, A dificuldade em ver que a coisa julgada pode ser invocada por terceiros, Revista dos Tribunais 1000 (2019), p. 425.

<sup>178</sup> See, for example: *Drahozal*, Class Arbitration in the United States, in: Hanotiau/Schwartz, Class and Group Actions in Arbitration (2016) p. 23.

<sup>179</sup> Strengthening the enforcement of shareholders’ rights (interim report) (2019), p. 20.



# 4. Report on derivative litigation and collective arbitration in Brazil

---

This chapter describes the Brazilian framework for derivative suits and collective arbitration proceedings, and subsequently proposes changes to Brazilian laws and regulations governing these two instruments. It builds on the conclusions and recommendations from Chapters 2 and 3. It was authored by Guilherme Setoguti J. Pereira, Professor, INSPER and IBMEC and Partner, Monteiro de Castro, Setoguti Advogados<sup>1 2</sup>

---

## 4.1. Introduction

This chapter was prepared to support the Brazilian Ministry of Economy and the Brazilian Securities Commission (Comissão de Valores Mobiliários – “CVM”) consideration of proposals to enhance the Brazilian law on (i) collective arbitration and (ii) derivative suits for imposition of liability on managers (directors and officers) and controlling shareholders under the Brazilian Corporation Law (“LSA”). Accordingly, this Chapter: (i) describes the Brazilian legal framework for derivative suits and collective arbitration proceedings; and (ii) proposes changes to the Brazilian laws governing these two issues.<sup>3</sup>

In March 2018 the Brazilian Ministry of Economy and the CVM created a working group (“WG”) and launched a project to improve investor protection in the capital market of the country through the improvement of private enforcement mechanisms of shareholder rights. The project is supported by the United Kingdom’s Prosperity Fund. The OECD also is providing technical support, which includes benchmarking Brazil against the rules and practices of other OECD members to help ensure that Brazil’s efforts to strengthen its framework and practices in this area are consistent with the G20/OECD Principles of Corporate Governance. The CVM and the OECD jointly prepared a Project Specification in June 2018 which established an initial scope for the project.

In October 2019 the WG, with the support of the OECD, published the “Strengthening the enforcement of shareholders’ rights – Interim Report” (“Interim Report”) as a product of the first phase of the project.

This Chapter has relied on the conclusions and recommendations from the Interim Report together with those written by Prof. Martin Gelter (Chapter 2), and Profs. André Monteiro and Renato Beneduzi (Chapter 3), prepared under the supervision of the OECD Secretariat. These two chapters respectively address the frameworks for derivative suits and collective arbitration in four Common Law jurisdictions (USA, UK, Singapore and Israel) and in four Civil Law jurisdictions (France, Germany, Italy and Spain). Chapter 3 also analyses the Portuguese framework for collective arbitration.

This work focuses on how these two instruments are dealt with when it comes to publicly traded joint stock companies (*sociedade anônima*), which are governed by the Lei das Sociedades Anônimas (“LSA”) and CVM regulation.

## 4.2. Derivative Lawsuits Under Brazilian Law

The LSA gives ample leeway to the controlling shareholders and to the managers (directors and officers) elected and guided by the former; however the LSA submits them to a stringent set of duties and responsibilities (LSA articles 116, 117, 153 through 158, and 245).<sup>4 5</sup> The LSA prescribes some lawsuits to put those corporate reins into practice, such as; (i) the liability suit against directors and officers (article 159); and (ii) the liability suit against the controlling shareholder (article 246):

*Article 159. By a resolution passed in a general meeting, the corporation may bring an action for civil liability against any officer for the losses caused to the corporation’s property.*

*Paragraph 1. The resolution may be passed at an annual general meeting and, if included in the agenda or arising directly out of any matter included therein, at an extraordinary general meeting.*

*Paragraph 2. The officer or officers against whom the legal action is to be filed shall be disqualified and replaced at the same general meeting.*

*Paragraph 3. Any shareholder may bring the action if proceedings are not instituted within three months from the date of the resolution of the general meeting.*

*Paragraph 4. Should the general meeting decide not to institute proceedings, they may be instituted by shareholders representing at least 5% of the capital.*



*Paragraph 5. Any damages recovered by proceedings instituted by a shareholder shall be transferred to the corporation, but the corporation shall reimburse him for all expenses incurred, including monetary adjustment and interest on his expenditure, up to the limit of such damages.*

*Paragraph 6. A judge may excuse the officer from liability, when convinced that he acted in good faith and in the interests of the corporation.*

*Paragraph 7. The action permitted under this article shall not preclude any action available to any shareholder or third party directly harmed by the acts of the officer.*

*Article 246. A controlling corporation shall be obliged to compensate any damage it may cause to a controlled corporation by any acts infringing the provisions of articles 116 and*

*Paragraph 1. Proceedings for compensation may be brought by:*

*(a) shareholders representing 5% or more of the capital;*

*(b) any shareholder, provided that he/she posts bond to secure payment of court costs in the event of the action being dismissed.*

*Paragraph 2. If the controlling corporation is held liable, in addition to paying compensation and costs, it shall pay an indemnity in respect of lawyers' fees at 20% of the compensation awarded and a further bonus of 5% payable to the plaintiff."*

When harmed by the actions of directors, officers or shareholders, the company is the proper plaintiff to bring these lawsuits, as Prof. Gelter (chapter 2 of this publication) mentions. However, as the company is represented by its directors and officers (LSA, article 144) who are elected – at least its majority – by the controlling shareholder, the authority given to minority shareholders to seek court relief in protection of the company works as an effective antidote to the risks of controlling shareholder abuse.<sup>6</sup> In other words, the company is guided by the controlling shareholders and represented by the directors and officers elected by the former which would make it very difficult for any measures to be taken against the managers unless the minority shareholders were vested with standing to sue.<sup>7</sup>

This circumstance makes *derivative suits* pivotal to a successful system of duties and responsibilities attributable to the controlling shareholder and to the managers.<sup>8</sup> It is against this backdrop that LSA provides for shareholder standing to sue on behalf of the company (article 159, paragraphs 3 and 4 and article 246, paragraph 1).<sup>9</sup> The shareholders who bring a derivative suit are a party to it, but as they are not the direct beneficiaries of the relief, any favorable outcome is awarded to the company.<sup>10</sup> The interests of the company are defended and the proceeds ultimately accrue to the company.

Differently from some legal systems, derivative suits in Brazil can only be brought to claim damages against the managers (directors and officers; LSA art. 159), the controlling shareholders (LSA art. 246) or a third party who assists the manager in the wrongdoing (joint liability; LSA, art. 158, paragraph 5). Similar limitations exist in France, Germany, Italy and Spain.<sup>11</sup>

Despite the importance the LSA grants to derivatives suits, studies have shown that they are usually regarded as an ineffective mechanism for redress<sup>12</sup> in Brazil. The studies have concluded that there is scarce litigation pursuing civil liability of managers and controlling shareholders.<sup>13</sup> Some of these studies have collected empirical data to support their assessment. One of them was conducted by Ana Carolina Rodrigues and found that civil liability suits are seldom used as an instrument to seek compensation from managers of listed companies. The study analyzed public data available and found 32 CVM administrative enforcement proceedings against managers of listed companies and only 11 liability suits against managers of listed companies within a given period in time. According to Rodrigues, that comparison suggested that investors and companies prefer to initiate an administrative proceeding rather than file a liability suit, possibly because the latter is more costly, ineffective and slow.<sup>14</sup> The problem with that finding is the fact that investors are not compensated in the CVM administrative proceedings, only in liability suits.

Another interesting empirical study, conducted by Viviane Muller Prado and Vinícius Buranelli, concluded that liability suits against managers and controlling shareholders are very infrequent if compared to other corporate and capital market disputes. The study found that, among 50 cases involving corporate issues within a given period, only 3 referred to liability of managers and controlling shareholders – which represents only 6% of the total of the cases analyzed.<sup>15</sup> Other papers of Prof. Prado present interesting data and conclusions that support the assumption that the Brazilian shareholders rights enforcement system is ineffective.<sup>16</sup>

The same conclusions can be drawn from collective claims. According to a study conducted by Lionel Zaclis, only 9 collective lawsuits had been filed based on the Law 7,913 during the course of 18 years following its enactment.<sup>17</sup> Another paper, issued in 2018, found that only 2 collective lawsuits involving listed companies' failure to supply information had been filed by the public prosecutor's office alongside the CVM, which acted as *amicus curiae*.<sup>18</sup>

### 4.3. Derivative lawsuits against managers (directors and officers) (LSA article 159)

LSA article 159 establishes four types of lawsuits in its main section and in paragraphs 3, 4 and 7. These lawsuits can be brought against directors and officers.<sup>19</sup>

Out of this total of four types of lawsuits, three are termed *corporate suits* (*ações sociais*) as they aim to safeguard the assets of the company and the results of a favorable award accrue to the company. These lawsuits can be brought by the company itself or initiated by shareholders, and are laid out in the main section of article 159 and in paragraphs 3 and 4, respectively. The shareholders can file the fourth type of suit (article 159, paragraph 7) in defense of their own assets. This work will focus on the suits presented in paragraphs 3 and 4, which can truly be called *derivative suits*.

Brazilian lawmakers have attempted to establish an optimal framework for derivative suits which discourages abuse<sup>20</sup> by weaving in a complex structure of *requirements* (eligibility conditions to be met) and at the same time creates *incentives* (stimulus to initiate a derivative suit). There are *requirements* for exercising the right to sue, such as a claim that the management of the company has failed to bring the suit after three months have elapsed since it was formally called upon to do so (LSA article 159, paragraph 3), along with the mandatory required ownership of at least 5% of the company's capital stock (LSA article 159, paragraph 4). There are also *incentives* for exercising the right to sue, such as the reimbursement of expenses in the case of a favorable outcome (LSA article 159, paragraph 5).

The Brazilian law requires a prior resolution adopted at a general shareholders meeting to file the corporate lawsuits set forth in the main section and paragraphs 3 and 4 of article 159. This resolution must be adopted by the majority of the votes represented in the general meeting (LSA article 129).<sup>21</sup>

In Brazil, the ordinary general meeting may approve the resolution even if this matter is not among the items on the agenda. This resolution can also be adopted at an extraordinary general meeting, provided that it is an express item on the agenda or directly derives from any discussion held in the general meeting (LSA article 159, paragraph 1).

The board of directors or the officers, subject to the bylaws, have the authority to call a general shareholders meeting (LSA article 123). The general meeting can also be called (i) by the audit committee ("Conselho Fiscal") if the competent administrative bodies delay doing so or in case of serious or urgent matters; (ii) by any shareholder in accordance with the law or the bylaws whenever the officers delay the call for more than 60 days; (iii) by shareholders representing at least five per cent of the capital if the managers do not comply within eight days with their justifiable request that a meeting be called, stating the matters to be discussed; or (iv) by shareholders representing at least five per cent of the voting capital or five per cent of nonvoting shareholders whenever the officers do not comply within eight days with the

request that a meeting be called to appoint a statutory audit committee.<sup>22</sup> There is no specific provision in Brazilian law regarding ownership requirements to include items on the agenda.

If the general shareholders meeting gives its green light to this action (resolution to sue), the management of the company must file the lawsuit (LSA article 159, main section) represented by its officers (LSA article 144). The officers will be in charge of the suit and the board of directors has a general duty of oversight, which includes monitoring the former. Brazilian law has no rule regarding the appointment of company's representatives or the formation of a special litigation committee as in other jurisdictions.<sup>23</sup> In this regard, Section 2.1.1.1 of the Interim Report explains that Brazilian Corporate Law does not regulate the *governance* of derivative suits:

“Brazilian Corporate Law does not regulate the governance of the lawsuit filed by the company against former managers. Pursuant to Article 144 of the Brazilian Corporate Law, the company is represented by its officers, including in the litigation against former officers or directors. Therefore, it is possible that managers do not have incentives to bring a lawsuit for compensatory damages against former colleagues and, even if they do bring it, there is no guarantee that they will apply the required resources and efforts in such lawsuits. In other jurisdictions, for example, claims initiated by minority shareholders were pursued by a court-appointed special representative. The WG understands that it would be advisable to pursue further studies on the matter, including by examining the existing governance rules in other jurisdictions in order to find a benchmark to be followed in Brazil.”

The law also establishes that the defendant managers become automatically disqualified and must be replaced at the same general meeting if the shareholders meeting approves the lawsuit (LSA article 159, paragraph 2). Spanish and Italian laws stipulate similar rules (– Chapter 2 of this publication).

If the company remains unresponsive and takes no action within three months after such resolution, any shareholder can initiate a lawsuit acting as nominal plaintiff for the company and seek redress in its favor (LSA article 159, paragraph 3). In Spain and Germany there are similar provisions but in Spain the company must pursue the suit within one month and in Germany the company must file within 6 months (Chapter 2 of this publication).

If the general meeting adopts a resolution against the filing of a derivative suit, any shareholder or group of shareholders representing at least 5% of the capital stock of the company may bring a derivative suit, also as nominal plaintiff for the company, and seek redress in favor of it (LSA article 159, paragraph 4).<sup>24</sup>

### **4.3.1. Exoneration from liability (*quitus*)**

The LSA establishes that the company must hold an ordinary general meeting annually within the first four months after the end of each fiscal year (as explained in Section 2.1.1 of the Interim Report). This ordinary general meeting is tasked with “taking the management accounts, as well as examining, discussing and voting on the financial statements”, among other matters (LSA article 132, I).

If the shareholders approve the financial statements and management accounts without qualification, the managers (directors and officers) are exonerated from liability for their conduct while in office during that year (LSA article 134, paragraph 3): “Unqualified approval of the financial statements and management accounts shall exempt the company's management and auditors from liability, except in case of error, willful misconduct, fraud or simulation (LSA article 286)”. This exonerating effect is known as *quitus*.

The rule establishes that liability is only imputable to the managers if, at the ordinary general meeting, the management accounts or financial statements (i) are rejected or (ii) receive qualified approval expressly stating that certain acts are actionable.

In the case of an unqualified approval, a lawsuit for damages is only possible if the general meeting resolution is (i) voided at the initiative of any shareholder on the grounds of an irregularity in such resolution, such as defective consent due to malice, error, simulation etc.<sup>25</sup>; or (ii) revoked by the company itself.<sup>26</sup>

Past court rulings have made it clear that prior annulment of an unqualified approval resolution is required for a damages suit to be filed within this context.<sup>27</sup>

#### 4.4. Issues for consideration/Recommendations

##### a) Eliminate or modify the exoneration from liability (*quitus*) upon approval of financial statements and management accounts as provided for in LSA article 134, paragraph 3.

Legal scholars have been criticizing LSA article 134, paragraph 3 for some time.<sup>28</sup> The financial statements and management accounts are not an actual rendering of accounts and are difficult to understand. Moreover, voiding a general meeting resolution on the grounds of defect of consent is seldom used, as this condition is difficult to prove.

Section 2.2.1 of the Interim Report explains that “This rule creates obvious procedural barriers to obtaining redress from the managers. First, even before filing the civil lawsuit, shareholders have to deal with the intricate problem of annulling the approval of the management’s accounts. Second, shareholders have to invest money and time to file the civil lawsuit against the manager with only the prospect to receive an indirect benefit, namely the restoration of the company’s assets. Third, there’s a difference in the statute of limitations of the lawsuit to annul the resolution that approved the managers’ accounts and financial statements and that of the civil lawsuit to hold managers liable, which may be interpreted as a decrease in the statute of limitation applicable to the latter”.

The Interim Report also explores how this subject is handled in other Civil Law jurisdictions:

*“In Germany (paragraph 120 of the German Stock Corporation Act) and in France (article L225-253 of the French Commercial Code) the approval of the managers’ accounts by the shareholders general meeting does not exempt the managers from liability. In Italy (article 2434 of the Italian Civil Code) and in Portugal (article 74° of the Portuguese Corporations Code) the approval of the management’s accounts also does not exempt managers from liability. However, exemption may be granted by an express resolution of the shareholders general meeting. In these latter examples a qualified minority (of 20% of the capital stock in Italy and of 10% in Portugal) has the right of veto. In Switzerland the approval of the management’s account only has an exception of liability effect regarding the facts expressly revealed to the shareholders general meeting, and even so shareholders who voted against still have the right to promote the derivative lawsuit to hold the managers liable (article 758 of the Swiss Code of Obligations). In Argentina the approval also has the exception of liability effect, except in the cases of breach of the law or the company’s bylaws provisions or if a qualified minority of 5% of the capital stock didn’t oppose the resolution (article 275 of the Argentinian Corporate Law)” (Section 2.1.1.1, footnote 33).*

In light of the above, the rule provided for in LSA article 134, paragraph 3 should be modified. One possible means would be to eliminate the rule. Consequently, consistent with the provisions in place in Germany and France, approval of the managers’ accounts would not exempt them from liability. A more incremental modification would be to amend the rule to read that only the facts expressly reported to the shareholders at the general meeting or by the official communication of the company would have exonerating effects. Consequently, the managers could be exempted from liability but would have to properly disclose the facts to provide the shareholders with the proper knowledge to vote with adequate information.

##### b) Consider creating a preliminary “pre-screening procedure” to decide on the admission of derivative lawsuits

The US, the UK, Germany, Singapore and Israel laws furnish some nature of pre-trial or admission procedure to decide on the admission of the derivative suit (Prof. Gelter (Chapter 2 of this publication)).<sup>29</sup> <sup>30</sup> These preliminary procedures call for a court decision using different criteria, such as demand futility, possible conflict of interest of the managers, best interests of the company, good faith, among other things. In these procedures, in Germany “the courts will look at the severity of the alleged breach of duty and whether the suit is in the interest of the corporation” (item 2.4.4).

Prof. Gelter argues that this preliminary procedure is one of the main factors for effective enforcement of derivative claims. This *screening mechanism* encompasses two main scopes.

The first is to decide on the acceptance of a derivative lawsuit. The mechanism weeds out abusive claims and permits the meritorious to move forward. This eliminates non-meritorious suits and claimants, thereby clearing the way for plaintiffs to proceed with good faith claims (Singapore) or grants the plaintiff with certain procedure rights, such as discovery (US).

The second scope is to limit the exposure of the plaintiff to financial litigation risk: “Success in a preliminary procedure can serve as a cutoff point after which the corporation (for whose benefit the derivative suit is brought) must bear litigation cost”. Jurisdictions that do not establish a pre-trial mechanism tend to expose the minority shareholders to the full financial litigation risk:

“A judicial screening mechanism following demand also has the advantage that shareholders’ litigation risk can initially be reduced to the cost of the preliminary stage. In fact, systems where shareholders can move directly to a derivative suit appear to be relatively little used. This may be explained by the fact that litigation fees (which plaintiffs will likely have to pay when the suit is unsuccessful) measured on the basis of the alleged harm to the corporation (and not only the plaintiff’s reflective injury) creates a strong deterrent. After a suit has passed the pre-screening stage, the law can provide for a different regime for cost. At that point, there is a strong justification for fees being paid by the corporation. Israel’s solution, where fees are set by the court, are an interesting innovation, as is the securities regulator’s ability to fund derivative litigation” (Prof. Gelter, Chapter 2 of this publication).

Perhaps Brazilian law should consider establishing a pre-trial lawsuit admission procedure to decide on the acceptance of derivative suits considering the two factors mentioned above. The shareholder who plans on presenting a derivative suit representing the company against the managers (LSA, art. 159) or the controlling shareholder (LSA, art. 246) would have to submit the claim to the competent court. The court would then assume the role of preliminarily assessing the merits of the claim according to criteria yet to be defined. The laws of the US (Delaware), the UK, Germany, Singapore and Israel use different criteria on this assessment, such as director’s conflicts of interest, the plaintiffs’ motives for the litigation (good faith) or if the suit is in the best interests of the corporation.<sup>31</sup> If the judge determines the claim meritorious and non-frivolous, the claimant would be entitled to certain procedures advantages, such as the company bearing the litigation costs or the court instructing the company to disclose documents relating to the derivative claim, among other aspects yet to be defined.

### **c) Consider eliminating or modifying the rule that demands the prior shareholders meeting to pursue liability**

As previously stated, Brazilian law requires a prior resolution adopted at a general shareholders meeting to file the corporate lawsuits outlined in the main section and paragraphs 3 and 4 of article 159. This aspect may not be in line with a large majority of the jurisdictions studied by Prof. Gelter.

According to Prof. Gelter, the UK, Israel and Singapore laws make no mention of involving the shareholders meeting in decisions to pursue liability. The Brazilian law prior resolution requirement also contrasts with the laws of Germany, Italy and Spain which explicitly *allow* shareholders to vote on bringing a lawsuit enforcing the responsibility of members of company organs, although Germany and Italian law do not *require* such resolution (and Spain requires the involvement of the shareholders meeting only under specific circumstances). France prohibits any clause in the articles of association that requires the shareholders meeting to approve a derivative suit or which may in some way waive the right of shareholders to bring such a suit (item 2.3 of the current document). Only in Spain must the shareholders first submit the issue to the meeting unless the allegation involves a breach of the duty of loyalty (item 2.3.2.1 of the current document).

The difficulties and disadvantages of mandatorily involving the general shareholders meeting with the decision to file a derivative lawsuit are also a subject of Prof. Gelter’s paper:

“Mechanisms involving the shareholder meeting, such as the ones discussed in this part, tend not to be frequently used to enforce directors’ liability. First, the relatively high percentage thresholds may be difficult to surmount for disgruntled minority shareholders. Second, the process to initiate litigation is cumbersome and likely results in valuable time being lost. Minority shareholders must add an item to the shareholder agenda, and then persuade the majority to vote in favour of the suit (Germany is the only of the three countries that gives a qualified minority the right to ask the court to appoint a special representative). Third, voting prohibitions cover only defendants themselves, but not other shareholders who supported the defendants. Thus, it is typically difficult to put together a majority in favour of the suit. Fourth, it is typically not attractive for shareholders to lose control over a suit to hand it over to (new) directors or a special representative that may not pursue the claim in accordance with their preferences. Thus, minority shareholders are more likely to use the actual derivative litigation mechanisms discussed in Section 2.4, where they are typically able to retain control” (item 2.3.3).

These findings demonstrate that the Brazilian rule is similar to that stated in Spanish law and may suggest that the former should be eliminated or, more reasonably, be modified to facilitate shareholder derivative proceedings without having to *mandatorily* obtain meeting approval.

As in other jurisdictions, perhaps the potential plaintiff in Brazil should have the *option* to submit the claim to the shareholder meeting to obtain certain effects, such as the disqualification of the defendant manager (LSA article 159, paragraph 2). But submitting the matter to the shareholder meeting would be an option and not a *mandatory requirement* as it currently is in Brazil.

#### 4.5. Derivative lawsuit against the controlling shareholder (LSA article 246)

The Brazilian law expressly allows the controlled company and the minority shareholders of the subsidiary to sue the controlling shareholder for damages. Under LSA article 246, the controlling entity must reimburse any damage caused to the company on account of actions taken in breach of LSA articles 116<sup>32</sup> and 117<sup>33</sup>. These legal provisions set out the duties of the controlling shareholder and exemplify the actions that may be regarded as an *abuse of controlling power*.

The controlled company itself can sue the controlling shareholder for damages. Nonetheless, it is improbable that the company will take action against the shareholder controlling it.<sup>34</sup> This circumstance adds further strength to derivative suits in this case as well. LSA article 246, therefore, authorizes minority shareholders to file a lawsuit on behalf of the company against the controlling shareholder without submitting the issue to a shareholders general meeting.

LSA article 246, paragraph 1 states that a suit for damages may be filed (i) by shareholders representing at least 5% of the company’s capital stock (item ‘a’); or (ii) by any shareholder regardless of ownership percentage upon posting of a bond for attorney fees and court costs possibly due if the claim is unsuccessful (item ‘b’). The first situation is similar to the rules provided for in certain states of the US.<sup>35</sup>

Similar to LSA articles 159, paragraphs 3 and 4, the shareholders are vested with standing to sue on behalf of the company: in the capacity of nominal plaintiff the shareholder is a party to the suit in defense of the company’s interests and the proceeds of a favorable award will ultimately accrue to the company.

If the suit is successful, the award must sentence the controlling shareholder to redress the damage and pay court costs, attorney fees at 20% based on the amount of the award and a penalty at 5% on top of the award to be paid exclusively to the shareholders who sponsored the suit (LSA article 246, paragraph 2). This provision operates as a legal incentive for this type of suit.

#### 4.5.1. Issues for consideration/Recommendations

- a) **Establish that any controlling shareholder can be the defendant in the lawsuit set out in LSA article 246: a company, an individual or any other entity (e.g., an investment fund)**

This modification is necessary because LSA article 246 reads that “the *controlling company* will be required to redress the damage (...)”, which may be construed as only a controlling *company* can be sued for damages caused to the controlled company. Even though LSA article 246 refers to a ‘controlling entity’ generally the suit for damages can be brought against any type of controlling shareholder.<sup>36</sup> The law should put this possibility in more precise terms to avoid misinterpretation.

- b) **Clarify that the lawsuit set out in LSA article 246 is not subject to the provisions outlined in LSA article 159 and no previous resolution at a general meeting is needed to file a suit of this type**

The suggestion is a required clarification because, even though LSA article 246 does not require a previous shareholders resolution to authorize the filing of the LSA article 246 lawsuit, some scholars and past court rulings (albeit the minority) have argued that the filing of a suit under LSA article 246 is subject to the rule in LSA article 159.<sup>37</sup>

Despite some dissonant opinions,<sup>38</sup> LSA article 159 does not govern the suit for damages against the controlling shareholder. The Superior Court of Justice (“STJ”) has demanded a prior general meeting resolution for the filing of a lawsuit against the controlling shareholder.<sup>39</sup> Nevertheless, the STJ itself has correctly determined at other times that the minority shareholders could sue the controlling shareholder for damages under LSA article 246 regardless of a prior general meeting resolution to that end.<sup>40</sup>

LSA article 246 does not refer whatsoever to a general meeting resolution which leads to the conclusion that such requirement has no legal grounds. But it is advisable that the law expressly states such position.

## 4.6. Cost of the proceedings

If the company is pursuing the claim directly against its managers or controlling shareholder, it will bear all the costs associated with the lawsuit. The same applies to shareholders acting on behalf of the company: if they decide to file a derivative suit, they will bear all the litigation costs (attorney fees, expert fees, court costs etc.).

If a lawsuit filed against the directors and officers by shareholders acting on behalf of the company is successful, those shareholders must be reimbursed for *all expenses* incurred, plus interest and adjustment for inflation, up to the amount of the award (LSA article 159, paragraph 5).

Lawsuits filed against the controlling shareholders are ruled by LSA article 246, paragraph 2 which establishes that, if the suit is successful, the controlling shareholders must pay the damages awarded to the controlled shareholders, plus *court costs* (and not *all expenses* incurred as set out in article 159, paragraph 5), 20% attorney fees and a 5% penalty, all based on the amount of the award.

These legal provisions show that the lawmakers strived to foster the filing of derivative suits by setting rules on financial incentives.

#### 4.6.1. Attorney fees

Attorneys and their clients agree by contract on the remuneration for legal services (*honorários contratuais*). In addition to these contractual fees, Brazilian law provides for loss-of-suit fees (*honorários sucumbenciais*) which accrue to the attorneys (Law 8,906/1994, article 23) and are owed by the defeated

party. Such provision is commonly referred to as the “loser pays” rule. All jurisdictions analyzed by Prof Gelter (Chapter 2 of this publication) adopt some form of a “loser pays” system, except for the US.

According to the Code of Civil Procedure (“CPC”), the judge must set the loss-of-suit fees at 10% to 20% of the (i) amount of the award; (ii) the economic gain obtained; or (iii) the amount of the initial claim adjusted for inflation if the gain cannot be measured (article 85, paragraph 2° of the CPC). The award must determine the rate taking into account the attorney’s dedication, the place where the service was rendered, the nature and relevance of the claim and the services performed by the lawyer as well as the time taken to perform such services (CPC article 85, paragraph 2°, I to IV).<sup>41</sup>

Brazilian law expressly states that the range of 10% to 20% is applicable regardless of the content of the decision and even when the judge dismisses plaintiff’s claims on the merits or dismisses the case without prejudice (CPC article 85, paragraph 6°).<sup>42</sup> This provision makes the 10% to 20% attorney fees rule applicable to the benefit of the lawyers of both the claimant and the defendant.

For claims in which the economic gain is inestimable or negligible, or when the amount of the claim is low, CPC article 85, paragraph 8° sets out that the judge must determine the amount of loss-of-suit fees employing an *equitable evaluation*. In these cases, the award must set the attorney fees under the criteria of article 85, paragraph 2°, items I to IV mentioned above.<sup>43</sup>

However, an intense debate has been taking place among scholars and courts concerning the applicability of the equitable evaluation rule. Some court rulings and part of doctrine defend the application of this rule in other situations beyond those outlined in CPC article 85, paragraph 8°.

Vast case law and doctrine sustains that the judge must always comply with the 10% to 20% rule except for those situations set out in article 85, paragraph 8°. This interpretation implies that if the defendant claims for BRL 1,000,000 the award must mandatorily set the loss-of-suit-fees between BRL 100,000 and BRL 200,000 both in cases of favorable and unfavorable rulings.<sup>44 45</sup>

On the other hand, some court rulings and scholars have applied the *equitable evaluation* rule not only in the situations mentioned in CPC article 85, paragraph 8° but also in other cases, especially when the attorney fees are considered abusive or insignificant.<sup>46 47</sup>

There is significant uncertainty on this matter as the Brazilian case law and doctrine still have not reached a consensus on the interpretation of these rules. More recently, STJ has been deciding that the equitable evaluation rule *must* be applied only in the situations set out in CPC article 85<sup>48</sup>, paragraph 85. Nonetheless, the lower courts have still been applying the equitable evaluation rule beyond those situations.<sup>49</sup>

In the situations in which there are multiple plaintiffs or multiple defendants, the losing parties must be proportionately liable for expenses and attorney fees (CPC article 87).<sup>50</sup>

It is also worth mentioning that these CPC provisions regarding attorney fees do not necessarily apply to arbitration proceedings, as the CPC is not automatically applicable to arbitrations. These rules will only govern arbitral proceedings if the arbitration convention stipulates so.<sup>51</sup> Therefore, the arbitral tribunal has no authority to award loss-of-suit fees unless stipulated by the parties. Moreover, even if the parties consent to the payment of attorney fees, the CPC rules do not bind the arbitral tribunal unless there is a specific agreement stating so. If there is no such agreement, the arbitrators can award the attorney fees following other criteria rather than CPC’s criteria.

#### **4.6.2. Bond**

Brazilian rules of civil procedure determine that the burden of advancing the litigation costs and expenses lies with the plaintiff, who upon a successful claim will be reimbursed by the counterparty.



In addition to this general responsibility to advance the litigation costs and expenses, LSA article 246 establishes (as seen above) that a liability suit may be brought against the controlling shareholder by the shareholders representing at least 5% of the company's capital stock or by any shareholder upon the posting of a bond as security for court costs and attorney fees which become due if the case is held groundless.

The law does not prescribe the amount of the bond. For that reason, the bond must be established on a case-by-case basis at a reasonable amount to cover loss-of-suit costs.

This bond requirement for filing a claim is an extraordinary measure prescribed by law under particular circumstances. Some legal scholars advocate that such bond stands as an *undue hindrance to the right of action* which goes against the constitutional right of unrestricted access to justice.<sup>52</sup>

### 4.6.3. Bonus

Payment of a bonus (*prêmio*) to the shareholder that took the initiative of filing suit to defend the interests of shareholders in general is amongst the existing incentives to that end. LSA article 246, paragraph 2, therefore, establishes that upon defeat the controlling shareholder owes the plaintiff shareholder a 5% bonus on top of the award in addition to the attorney fees set at 20%.

The law prescribes the payment of the 5% bonus and the 20% attorney fees only for suits against the controlling shareholders (LSA article 246) and not for suits against managers (LSA article 159). For the latter, there is no provision regarding the payment of a bonus and the attorney fees must be calculated pursuant to the regular rules of the Code of Civil Procedure, as previously seen in this Report.

It is worth noting that despite opinions that the judge is not obliged to set 20% attorney fees as set out in LSA article 246, paragraph 2,<sup>53</sup> this is indeed a mandatory percentage expressly prescribed by law. Thus, in case of a favorable decision the judge must award attorney fees at 20% on top of the award. This rule has the potential to create a strong incentive for parties and their lawyers to bring the suit, even though there are no empirical studies to support the assumption that such incentive has properly worked.

The LSA does not prescribe a rule regarding how to divide the 5% bonus in cases with several plaintiffs. The attorney fees, on the other hand, must be proportionately divided among the winning parties' attorney according to the criteria set out in CPC article 87 as previously explained in this Chapter.

## 4.7. Issues for discussions/Recommendations

### a) Unify the systems for reimbursement of expenses for the lawsuits brought under LSA articles 159 and 246

There is an aspect worth noting in the legislative rules governing the expenses incurred with derivative suits: a *regulatory disparity* in the legal approach to this matter by according a differing treatment of similar situations. The legal provisions on derivative suits suffer from inconsistency.

This aspect can be seen in LSA article 159, paragraph 5 which provides for redress of *all expenses* incurred with the case plus *interest and adjustment for inflation*. For its part, LSA article 246, paragraph 2 provides for payment of *court costs* only without any reference whatsoever to other expenses, such as interest or adjustment for inflation. What was the rationale of the lawmakers for such a distinction?

The two claims should have been afforded the same provisions as they all lead to the same: a shareholder acting as nominal plaintiff of the company seeking payment for damages that will ultimately accrue to the company if successful. In all those suits, a plaintiff shareholder is individually acting for the benefit of a common interest, and they are all subject to the same rationale of concentrating the costs and spreading the benefits. Therefore, they should also be governed by the same provisions – preferably those set out in

LSA article 159, paragraph 5 which is more comprehensive by determining the reimbursement of *all reasonable expenses* incurred with the case including interest and adjustment for inflation.<sup>54</sup>

- b) Modify the rule set out in LSA article 159, paragraph 3, to establish that when a shareholder brings a suit on account of the company's unresponsiveness, the latter must bear all costs of litigation regardless of its outcome.**

There should be full reimbursement of the costs in the event of LSA article 159, paragraph 3, when the general shareholders meeting has adopted the filing of a suit (resolution to sue) but the management has failed to comply, thereby forcing the shareholder to claim as a nominal plaintiff of the company. The company should reimburse the costs regardless of the outcome of the suit in these cases.<sup>55</sup>

This suggestion is in line with the Interim Report recommendations: "In view of the above, the WG considers that the provisions of the Brazilian Corporate Law should be amended to: provide that plaintiffs will be entitled to reimbursement of all the costs incurred when the lawsuit was approved by the shareholders general meeting and the managers fail to take the proper measures" (Section 2.1.1.2 of the Interim Report).

The same logic for this suggestion is present in other jurisdictions in which the corporation must compensate the shareholder acting on its behalf regardless of the outcome. For example, Prof. Gelter's Chapter explains that in Germany "if the suit advances past the preliminary stage, shareholders are compensated for their cost even if it is unsuccessful, unless the shareholder supported the application with false information and in doing so acted intentionally or with gross negligence". In Israel, "if a derivative suit is approved by the court, the company must compensate the plaintiff for his fees. It may also order the company to advance him future payments and hold it liable for the defendants' expenses" (item 2.4.6 of Chapter 2).

Another aspect in need of attention is the burden of harmed shareholders bearing the expenses in advance which are only recovered *at a later date and if the lawsuit is successful*. The harmed shareholder is forced to advance all expenses and will only be reimbursed several years later if a favorable outcome is obtained.<sup>56</sup>

Perhaps an advancement of costs by the company itself should also be considered. After all, the general meeting had adopted a resolution to sue and the company did not file the lawsuit because of management's failure. In such situation one should perhaps consider the possibility of the company advancing expenses instead of only reimbursing them at the end of proceedings.

If the Brazilian law adopts a preliminary procedure for the admission of derivative suits, as discussed in item 4.4.(b) of this Chapter, then the reimbursement by the company of the reasonable litigation costs should also be considered if the plaintiff is successful in a preliminary stage.

- c) Extend the attorney fees and bonus payment provisions under LSA article 246 to the lawsuit laid out in LSA article 159**

The 5% bonus and the 20% attorney fees set out in LSA article 246 are justifiable not only in the context of lawsuits brought against the controlling shareholder but also for those against the managers.

It seems somewhat incoherent to provide for a 5% bonus solely with a lawsuit under LSA article 246 while failing to do so for one under LSA article 159. Why should this bonus not be imposed in the context of a lawsuit brought against the directors and officers of the company? The law should extend this incentive mechanism to all lawsuits brought in defense of the interests of the company, including the liability suits against directors and officers (LSA article 159).<sup>57</sup>

This suggestion reflects the Interim Report recommendations: "In view of the above, the WG considers that the provisions of the Brazilian Corporate Law should be amended to: create a premium for shareholders who file the derivative lawsuit in case of a favorable ruling" (Section 2.1.1.2).

**d) Expressly state that the 20% attorney fees and the 5% bonus accrue on the *total amount of the award* and not only on the amount that is proportionate to the ownership of the shareholder**

Contrary to what LSA article 246, paragraph 2° establishes, the STJ has already ruled that the 5% bonus and the 20% attorney fees should be calculated not on the total amount of the award but rather on the plaintiff shareholder's ownership percentage multiplied by the amount of the award.<sup>58</sup> If this rationale prevails over the express wording of the rule it would deal a heavy blow to the existing incentive for shareholders to defend the interests of the company.

This amendment is necessary to clarify the existing legal rule and to eliminate the interpretations by the mentioned court rulings.

**e) Discuss modifying the “loser pays” rule to foster derivative suits**

The financial risks arising out of the proceedings are one of the fundamental reasons that discourage minority shareholders from filing derivative lawsuits on behalf of the company. The plaintiff acts in the benefit of a common interest and, if the indemnification is granted, it will accrue to the company. Accordingly, the plaintiff bears all costs and risks of the litigation but will receive only an indirect and proportionate benefit if the case is successful.

The rationale behind the defeated litigant paying court costs is to discourage frivolous litigation. The other side of the coin is that such rule can also discourage legitimate claims from those in possession of a valid substantive right for which relief could be sought in court (under-deterrence).<sup>59</sup>

This concern is particularly relevant in jurisdictions that adopt the “loser pays” rule since the plaintiff bears not only the costs of its lawyers and experts but also reimburses the counterparty for costs if the case is dismissed. This is especially burdensome in Brazil, where the rules of the Code of Civil Procedure determine that the loser must reimburse the winning party court costs and also pay attorney fees between 10% to 20% on top of the claim (article 85, paragraph 2°). Brazilian case law is controversial as to whether the attorney fees must always be in accordance with this rule or can be set by *equitable evaluation* (article 85 paragraph 8°). Consequently there is a considerable risk that the shareholder will have to pay 10% to 20% of the claim.

The “loser pays” rule as laid out in the Brazilian civil procedure law system deters the filing of claims,<sup>60</sup> especially those involving representative capacity matters in which the claimant would obtain indirect benefits that are disproportionate to the total relief being sought: besides the contractual fees payable for being represented by a lawyer, the claimant could also be sentenced to pay loss-of-suit fees to the attorney of the counterparty.

This aspect of Brazilian law undoubtedly discourages shareholders from filing lawsuits as representatives of the company and should be addressed to foster derivative litigation in the Brazilian capital market.

If the Brazilian law adopted a preliminary procedure to decide on the admission of derivative suits and if the claim is cleared as discussed in item 2.1.2.(b) of this Chapter, then the reimbursement of the reasonable litigation costs by the company, including attorney fees, should also be considered by Brazilian lawmakers.

A second possible solution would be to cap the attorney fees for unsuccessful derivative lawsuits. The judge would not calculate the attorney fees at 10% to 20% of the award, but at much lower rates established by law.

Exempting the plaintiff from paying attorney fees except in case of bad-faith or frivolous claims is a third possibility that should be taken into consideration. This rule would be similar to articles 17 and 18 of Law 7,347/1985 which states that if an association initiates a class action (*ação civil pública*) and the case is

dismissed the plaintiff must not be condemned to pay attorney fees and other costs of the proceedings except in case of bad faith.<sup>61</sup>

#### 4.8. Minimum ownership thresholds (LSA article 291)

LSA article 159, paragraph 4 and article 246, paragraph 1(a) establish a minimum ownership interest for eligibility for certain lawsuits. These threshold requirements reflect the concerns of lawmakers with *strike suits*,<sup>62</sup> i.e. frivolous derivative suits of questionable merits that are filed by minority shareholders disregarding the interests of the company itself.

Under certain circumstances these minimum eligibility conditions may entail an almost insurmountable obstacle, which is more evident in companies with dispersed capital.

LSA article 291 therefore states that the CVM may reduce the percentage thresholds stated in LSA article 159, paragraph 4 and article 246, paragraph 1 (a)<sup>63</sup> in a manner proportionate to the capital stock of the company.

As the Interim Report refers,<sup>64</sup> in October 2019 the CVM opened public comment for a proposed rule on the minimum ownership percentages (proportionately to the company's capital stock) for filing claims under LSA article 159, paragraph 4 and article 246, paragraph 1(a)<sup>65</sup>.

CVM received several comments on the proposal and on June 22<sup>nd</sup>, 2020 issued Instrução CVM 627, establishing a regulation on the matter:

Table 4.1. CVM rule on the minimum ownership percentages

Capital Stock (BRL)	Minimum Threshold (%)
Between 0 and 100 million	5
Between 100 million and 1 billion	4
Between 1 billion and 5 billion	3
Between 5 billion and 10 billion	2
Above 10 billion	1

#### 4.9. Issues for consideration/Recommendations

##### a) Give the CVM greater leeway to change the percentage ownership interests set out in LSA article 291 by considering criteria other than the capital stock

The content of LSA article 291 could be enhanced as mentioned in Section 2.1.1.1 of the Interim Report. The prescribed percentages seem to have been chosen at random. What is the rationale behind the 5% threshold? Why not 1%, 3% or 10%?

The second aspect of improvement has to do with the grounds in LSA article 291 for reducing the threshold percentage: the capital stock. Criteria better reflecting a company's ownership dispersion should also have been included in LSA article 291 for a reduction in the threshold percentages. It would be advisable that LSA article 291 give the CVM some leeway to reduce the threshold percentages after considering the capital stock and other factors such as extent of stock dispersion, or the existence of a defined controlling entity.<sup>66</sup>

According to Prof. Gelter's Chapter, even the thresholds presented in Table 4.1 might be higher than those applied in other jurisdictions. In the same way, if a preliminary procedure to decide on the admission of

derivative suits is proposed to reduce the possibility of frivolous derivative lawsuits, one should also evaluate the option of abolishing any threshold for proposing a derivative lawsuit.

#### **b) Contemporaneous and continuous ownership of stock**

There is no requirement under Brazilian law regarding contemporaneous and continuous ownership of stock of the harmed company at the time when the wrongdoing was committed or when the court decision is rendered.

Brazilian legal scholars and court rulings have seldom dealt with this matter, which may indicate that it might have little relevance in practice. But it has already started to come up in some disputes as in the Braskem/Odebrecht case, which discusses the controlling shareholder's liability under LSA article 246. One of the defence arguments is that the nominal plaintiff was not the owner of shares in the controlled company at the time of the alleged wrongdoing (Case No. 1097498-46.2018.8.26.0100, in course at the 2nd Lower Corporate and Arbitration Court in the Judicial District of São Paulo).

Prof. Gelter's Chapter explains that these rules are not found in most jurisdictions under examination (item 2.4.3 of Chapter 2) and questions whether they are recommended or not:

"The contemporaneous ownership requirement also seems questionable, as it is not entirely clear why trading in probabilistic claims should be prohibited. In the United States the historical reason for its original introduction was that the federal courts wanted to put an end to the practice of transferring stock in order to create diversity jurisdiction. The requirement thus seems only justifiable where forum shopping is a considerable risk. The 'continuous ownership requirement' seems less problematic. It seeks to ensure that the plaintiff's incentives are aligned with those of all shareholders. However, given that the actual driving force behind a suit is usually an attorney who stands to gain from a successful suit or settlement, it is not clear why it should be necessary".

Therefore, we face two central questions in relation to the issue: (i) whether the law should require contemporaneous and continuous ownership of stock of the harmed company at the time when the wrongdoing until the court decision is rendered; (ii) in either case, if the law should be amended in order to clarify which rule applies in Brazil.

### **4.10. Subsequent control over a derivative suit and settlements**

Unlike Brazil, some jurisdictions set forth specific rules regarding settlements in derivative suits. The laws of Singapore, Israel and the UK, for instance, prescribe some sort of participation of the courts in the settlements: while in the first two countries the courts *must* approve all settlements, in the UK the courts *may* intervene in the settlements at its own discretion.

On the other hand, German, Italian and Spanish laws require the shareholders to vote in the general meeting "to renounce or settle a directors' liability claim" and grant the minority shareholders the right to block a settlement. Moreover, in Germany a settlement is possible only three years after the claim arose. French law provides that the shareholders meeting is powerless to stop a derivative suit initiated by a shareholder (Prof. Gelter – Chapter 2 of this publication).

The LSA does not have any provision regarding the requirements for settling or waiving a derivative claim. Despite the lack of specific rules under the LSA, the shareholder cannot settle or waive the claim in a derivative suit, given that he or she is acting on behalf of a right of the company. The nominal plaintiff is vested with standing to sue on behalf of the company but has no authority to waive the company's rights. Therefore, the doctrine states that any agreement executed by the shareholder without the consent of the company will not bind the latter.<sup>67</sup>

Perhaps the Brazilian lawmakers should consider establishing a rule demanding that settlements must be approved by the court or by the shareholders, which could also include granting minority shareholders the right to veto the decision.

#### 4.11. Mechanisms to reduce the information asymmetry among shareholders, the company, the controlling shareholder and managers

Effective evidence production mechanisms are of great importance for the success of a derivative lawsuits system, because of the asymmetry of information that exists among the minority shareholder and the company, the managers and the controlling shareholder. In other words: one of the requisites for an effective shareholders protection system is for the investors to have proper information and means to produce evidence of the wrongdoing and its consequences (i.e., damages).<sup>68</sup> These issues are addressed in Prof. Gelter (Chapter 2 of this publication).

That is the reason why Guido Ferrarini and Paolo Giudici state that *discovery*<sup>69</sup> is an essential mechanism in litigation involving corporate and capital market disputes. They further state that in civil law European countries without mechanisms such as discovery it is virtually impossible to prove complex misconduct, due to the barriers with obtaining documents that are in possession of the counterparty, except if the information and the documents are obtained by a public authority.<sup>70</sup> A similar position is defended by other authors, who consider that the discovery is one of the main elements responsible for the success of the US shareholders protection enforcement system.<sup>71</sup>

Like most other civil law jurisdictions, Brazil does not have broad production of evidence mechanisms such as the US-style discovery. The Company Law prescribes which documents the shareholders have the right to access and the CPC provides for procedural tools for obtaining documents. However, these mechanisms are not effective and case law is somehow uncertain about the interpretation of those provisions and about which documents the shareholders can access, especially with regard to listed companies.

Brazilian experts should consider establishing mechanisms that allow the shareholders to access documents that are in possession of the company, the controlling shareholders or the managers, especially if the shareholders provide the court with reasonable elements that show, at a *prima facie* analysis, the claim is meritorious, and prove that they have tried to access the documents before going to court.. However, there should be concerns with *abuse* of the right to access documents (fishing expedition), and the best way to deal with this issue seems to be the UK and Israeli approaches.

As explained by Prof. Gelter, some jurisdictions are furnishing instruments to facilitate the gathering of information specifically for derivative suits. The UK is one example: where the court “may give directions as to evidence provided by the company”, upon the failure of the plaintiff to establish a *prima facie* case for a derivative suit. In Israel a potential plaintiff of a derivative claim may ask the court – before the filing – to instruct the company to “disclose documents relating to the process of approving the derivative claim. The court may approve such an application if it is persuaded that the plaintiff has provided preliminary evidence regarding the existence of the conditions for admitting a derivative suit” (Prof. Gelter, Chapter 2 of this publication).

The best way to provide the shareholder with information and at the same time to prevent *discovery abuse* is to grant the plaintiff with reasonable production of evidence under supervision of the court or the arbitral tribunal, provided that the plaintiff shows preliminary evidence of the wrongdoing and proves that they have tried to obtain the documents before requesting the judicial or arbitral order. In other words, the shareholder should be granted a broader access to evidence if it presents *prima facie* evidence of the facts that justify the derivative suit.

This suggestion is in accordance with the conclusions of Prof. Gelter: “The discussion following this chapter is unlikely to result in the introduction of US-style discovery, which would likely face fierce resistance in many parts of the world because it is considered alien to the legal culture and an abuse litigation practice. However, among the instruments surveyed in this section, the relatively recent legislative innovations in the UK and Israel seem promising. They are both tied to the preliminary screening procedures in these courts, which means that the court has tight control over which plaintiffs will be given a leg up in order to overcome the severe information problems in collective litigation. This should ensure that discovery procedures are not abused by plaintiffs going on fishing expeditions” (See Section 2.5).

Another way to deal with the mentioned information asymmetry is the shift in the burden of proof, similar to what is provided by German law, where the members of the management or supervisory board may have the burden to show that they complied with the proper standard of care (Prof. Gelter, Chapter 2 of this publication). In Brazil article 373 of the CPC states that “In the cases provided for by law, or in view of the peculiarities of the action relative to the impossibility or excessive difficulty of performing the duty pursuant to the head provision, or even the greater ease of obtaining evidence to the contrary, the judge may assign the burden of proof differently, provided this is done in a reasoned decision, in which case the party must be given the opportunity to carry out the assigned charge”. As we have defended in previous work, corporate and capital market disputes are a conducive for the application of this provision because of their information asymmetry.<sup>72</sup>

## 4.12. Collective Arbitration Under Brazilian Law

### 4.12.1. Corporate and Capital Market Arbitration in Brazil

Brazilian legal scholars and lawmakers have made great strides in improving the country’s capital markets since the late 1990s and early 2000s by enhancing the corporate law framework and putting in place a more reliable system for investor protection.<sup>73</sup>

In this spirit of reform, Law No. 10,303 of 2001 and Law No. 10,411 of 2002<sup>74</sup> introduced, among other changes, paragraph 3 to article 109 of the LSA expressly providing for the inclusion of an arbitration clause in the company’s bylaws (for resolution of disputes between the shareholders and the company, or between the controlling and minority shareholders).

The Bolsa de Valores de São Paulo – Bovespa (currently, B3) followed suit and decided in 2000 (i) to institute various corporate governance levels (*Novo Mercado, Nível 1* and *Nível 2*) designed to foster a more attractive securities trading environment by raising the bar on corporate governance practices that went beyond those prescribed by law,<sup>75</sup> and (ii) to make arbitration compulsory for dispute resolution involving shareholders, managers and companies trading at the two highest governance levels (*Novo Mercado* and *Nível 2*).<sup>76</sup> In 2001 Bovespa set up the Market Arbitration Chamber (“CAM-B3”) with the purpose of contributing towards enhancing the Brazilian stock market.<sup>77</sup> Section 3.2 of the Interim Report<sup>78</sup> and Profs. Monteiro and Beneduzi’s Report (Chapter 3 of this publication)<sup>79</sup> present interesting statistics about the activities of the CAM-B3. Studies have shown that corporate disputes are the most common subjects of arbitration in Brazil and represent, in some arbitration chambers, up to 40% of their proceedings.<sup>80</sup>

These initiatives sought to supply the country’s stock market with adequate enforcement tools that were viewed as vital to its development.<sup>81 82</sup> The installation of specialized arbitration centers was promised to lead to a more suitable resolution of corporate conflicts.<sup>83</sup> This measure taken by the private regulator relied on the assumption that arbitration is an excellent (if not the best) means for corporate dispute resolution conflicts in the capital markets.

The Code of Best Corporate Governance Practices of the Brazilian Corporate Governance Institute (IBGC) establishes that corporate conflicts should be settled by negotiation between the parties or, if not possible, by mediation and/or arbitration.<sup>84</sup> The CVM's Corporate Governance Guide also suggests that corporate disputes should preferably be resolved by arbitration.<sup>85</sup>

In initiating these reforms, public and private regulators signaled that arbitration goes hand in hand with the highest standards of corporate governance and, consequently, is an effective tool to protect the interests of minority shareholders and investors. By extension, companies with bylaws containing an arbitration clause would be more prone to receive investments.

However, legal scholars until recently were split as to whether the arbitration clause set out in the company's bylaws as per article 109, paragraph 3 of the LSA bound the shareholders as well.

Law No. 13,129 of 2015 sought to shed light on this matter by adding article 136-A to the LSA. The article states that all shareholders are bound by the arbitration clause and, in turn, provides dissenting shareholders with a right to withdraw. The article states that this right to withdraw does not apply only if the choice for arbitration was a condition for the company's eligibility to a special listing segment of stock exchanges or organized over-the-counter markets, or if the company stocks are highly liquid and widely dispersed (LSA article 137, I(a) and (b)).

This legislative change has further cemented the choice of arbitration as a mechanism for alternative resolution of corporate disputes involving listed companies. However, it is also important to note that a significant number of listed companies that have not adhered to a special listing segments requiring the use of arbitration still have chosen not to make it their preferred choice to resolve shareholder disputes. Legally, it remains a voluntary mechanism not required by law, but only if a company wishes to subscribe to certain listing segments, or voluntarily designate arbitration as the means for settling disputes by changing their bylaws.

The Brazilian scenario and experience regarding corporate and capital market arbitration are unique. Brazil differs from other countries, as explained in Section 3.2 of the Interim Report:

*"The issue of mandatory arbitration provisions in the bylaws is a highly controversial topic, and the Brazilian position of allowing arbitration to solve disputes involving capital market players (including publicly-held companies) does not find support in other jurisdictions usually seen as reliable benchmarks, such as Germany, Italy, Israel, and Sweden.*

*In such countries, in general, arbitration is considered inappropriate for publicly-held companies, and the discussion about the use of arbitration to settle corporate disputes involves other corporate types. In a prima facie analysis, in fact, no jurisdiction with a legal system similar to Brazil's (Civil Law) has regulated the use of arbitration in disputes involving or related to publicly-held companies.*

*This debate also exists in Common Law countries. In the United States, for instance, the inclusion of mandatory arbitration agreements in North-American publicly-held companies' bylaws, until this moment, has not been expressly authorized by the SEC".*

Chairman Jay Clayton of the Securities and Exchange Commission has stated that "the ability of domestic, publicly-listed companies to require shareholders to arbitrate claims against them arising under the federal securities laws is a complex matter that requires careful consideration" and "if the issue were to arise in an actual initial public offering of a domestic company, it would not be appropriate for resolution at the staff level but would rather be best addressed in a measured and deliberative manner by the Commission."

Other U.S. agencies, however, have supported the use of arbitration in securities litigation. For example, the U.S. Department of the Treasury issued a report in October 2017 suggesting that mandatory arbitration should be used as a tool to reduce the costs of shareholder litigation. It recommended that the states and the SEC continue to investigate the various means to reduce costs of securities litigation for issuers in a



way that protects investors' rights and interests, including allowing companies and shareholders to settle disputes through arbitration.

As stated in Section 3.2 of the Interim Report, "these facts sparked a vigorous discussion about the practical effects that mandatory arbitration agreements would have on shareholders' ability to adequately vindicate their rights under the U.S. securities laws, possibly depriving them of important federal rights to litigate securities fraud violations in court. According to a recent article published on the Harvard Law School Forum on Corporate Governance and Financial Regulation, "many scholars and advocates have concluded that the potential harm to investors of being forced to arbitrate securities violations significantly outweighs such benefits".

These barriers are mainly related to information asymmetry (which derives from the confidentiality of the arbitral proceedings) and cost of the proceeding issues. These issues will be addressed in the following sections of this Chapter.

#### **4.12.2. Collective Arbitration**

One of the major problems faced in capital markets wrongdoing disputes is that the damage suffered by investors from an individual standpoint usually involves insignificant amounts. Therefore, it is not uncommon that the only economically feasible means of recovery is to engage in group litigation via collective mechanisms.<sup>86</sup> This is the very reason why the class action operates as the primary mechanism for private enforcement of capital market regulations under US law.<sup>87</sup>

As Section 2.1.3 of the Interim Report describes, the Brazilian legal system has provided for collective protection of investor rights in the securities market<sup>88</sup> since the enactment of Law 7,913 in 1989. But only a few class actions have been brought in reliance on such law.<sup>89</sup> In fact, Brazil is not alone in this dilemma: apart from the United States and a handful of other common-law countries, class actions defending capital markets interests are, in the words of John Coffee Jr., *as rare as unicorns*.<sup>90</sup>

Law 7,913/1989 establishes that civil public actions (*ações civis públicas*) may be filed to protect the interests of the investors themselves (termed 'homogenous individual interests') as well as diffuse and collective interests.

The Public Prosecutors Office has exclusive authority to file a class action as per article 1 of Law 7,913/1989. Notwithstanding, in light of article 3 of the same law, several legal scholars and past court rulings have defended that all entities listed in article 5 of Law 7,347/1985 have standing to file a class action as well. As a result, the CVM<sup>91</sup> and associations, among others, are determined to have standing to sue. The law more specifically states that associations must list amongst their core objectives the protection of the securities holders rights and must also have been set up at least one year before the filing date (article 5, V(a) and (b) of Law 7,347/1985; article 82, IV of the Consumer Protection Code). The judge may opt to dispense with this latter requirement if there is a community interest in the claim on account of the extent or characteristic of the damage or due to the relevance of the legal right for which court relief is sought (Consumer Protection Code, article 82, paragraph 1).

It is within this context that Brazil is currently discussing the matter of collective arbitration as well as in light of the clear intention of Brazilian lawmakers to foster arbitration as a method of choice for the resolution of corporate disputes. In reality, some collective arbitration proceedings have even been initiated by investors against Brazilian companies over the last years.

Scarce information is available since these proceedings are not public. However, public databases cite at least seven collective arbitrations currently underway in Brazil.

The 2019 Reference Form of *Petróleo Brasileiro S/A - Petrobras* (Petrobras) reports that "Petrobras is a respondent in five arbitration proceedings installed by Brazilian and foreign investors in the Market Arbitration Chamber linked to B3 – Brasil, Bolsa, Balcão".<sup>92</sup> Further, according to the press, in July 2019

investors commenced arbitration against Vale S/A (Vale) on account of the Brumadinho tailings dam collapse.<sup>93</sup> Vale's 2019 Reference Form and Material Fact do not refer to such arbitral proceeding though.<sup>94</sup> More recently the press also informed that investors commenced a collective arbitration against IRB – Instituto de Resseguros do Brasil.<sup>95</sup>

The Brazilian legal system has yet to come to grips with this recent trend. The Arbitration Act has no rule dealing with collective arbitration matters and provisions of leading arbitration centers in Brazil<sup>96</sup> are also silent in this specific regard. The Arbitration and Mediation Chamber of the Federation of Industries of the State of Paraná (“CAMFIEP”) arbitration rule stands alone in an effort to tackle the issue of addressing the rights of representation in an arbitration commenced by associations.<sup>97</sup>

As seen before, when the subject is collective and corporate arbitration, Brazil is unique in two ways. First, since the beginning of the years 2000, Brazil has been choosing to submit our corporate disputes to arbitration, especially those regarding listed companies. As explained by Profs. Monteiro and Beneduzi's Chapter, only Spain has adopted arbitration as a means of solving corporate and capital markets disputes. Second, Brazil does have ongoing collective *corporate* arbitral proceedings. The US is the only country analyzed by the chapter with collective arbitration, but no collective *corporate* arbitration. Brazil may learn from other countries' experiences. However, we must keep in mind that Brazil faces a very unique and peculiar situation and that we are facing unknown ground with collective corporate arbitration.

There are four fundamental issues this chapter raises before addressing the concrete proposals related to collective corporate arbitration in Brazil.

First, is arbitration truly the best method of resolving corporate and capital markets disputes, as mentioned above? Since early 2000s, Brazil has chosen to submit its corporate disputes to arbitration. This choice was made by the lawmakers, by B3 (then Bovespa) and by the legal scholars. Brazilian arbitration is strongly associated with high levels of corporate governance and investor protection. But now some scholars are beginning to question if that arbitration choice was correct and if Brazil has gone too far. There are reasons to question the assumption that arbitration is *always* the best means to solve corporate and capital market disputes: arbitration is costly, confidential, not as fast as we would like it to be, and presents other transactional costs. If it is not adapted to address the characteristics of collective disputes, arbitration may represent more of a barrier than a facilitator to access to justice, at least when dealing with capital markets disputes.

The second fundamental question is: do we want to apply to collective arbitration the same rules that govern our judicial collective suits system (*ações civis públicas*)? The Brazilian judicial collective suits system has peculiarities, including regulation on standing to sue and *res judicata*, among others. There is a relative consensus among scholars and lawyers that the Brazilian collective suits system does not work as it should. There have been some legislative initiatives, and some scholars have drafted bills of law. But none of them have succeeded and they have all been stuck in the Congress for years. Therefore, it would be a natural conclusion to suggest that we should take this opportunity to create a new, parallel and better collective (arbitration) system. But we must also be fully conscious of the side effects of having two different collective systems coexisting in the same jurisdiction.

This gets us to the third fundamental question: if Brazil decides to move forward with a collective arbitration system, will we establish statutory/legal provisions or will we delegate this task to the arbitral centers? Among the countries analyzed in chapter 3, only the US has collective arbitration provisions, but these provisions are all laid out in the arbitration center regulation and not in the law. What would be the best approach for Brazil? This question will be addressed below and is a crucial and strategic question of politics.

The fourth fundamental issue is: if we do decide to proceed with a collective arbitration system as a means of solving capital markets and corporate disputes there is no doubt that we need to address the confidentiality issue. It is inconceivable to think about confidentiality with any collective rights system, be it

judicial or be it arbitral. In any situation, the market and the members of the class must be aware of what is being discussed in collective suits. Information is one of the pillars of any collective system.

### 4.13. Confidentiality

Brazilian law requires that the arbitrator's conduct be discreet during the course of arbitration (Brazilian Arbitration Act, article 13, paragraph 6). However, it stands to reason that arbitration and confidentiality are not necessarily intertwined<sup>98</sup> as there is no reference in the law to a confidentiality duty attributable to the parties in arbitration proceedings.<sup>99</sup>

In spite of this omission, confidentiality is generally cited by legal scholars<sup>100</sup> and litigants<sup>101</sup> alike as one of the major advantages in referring a dispute to arbitration in lieu of the Judiciary. Following the same line of reasoning, the agreements to arbitrate as well as the rules of arbitration bodies generally mandate that the arbitration must be secretive.<sup>102</sup>

Article 9.1 of the Arbitration Rules of the CAM-B3, for instance, reads that “the arbitration proceeding is confidential, and the parties, arbitrators and members of the Arbitration Chamber shall abstain from disclosing information on its content, save for compliance with the rules of regulatory bodies or by operation of law.”<sup>103</sup> The Internal Rules of CAM-B3 support the rationale and add that (i) the arbitration proceedings under its administration “must be kept secret” (article 6.1), (ii) the General Secretary must ensure that the arbitration is being accorded a confidential treatment (article 3.3, (d)), (iii) the chair of the CAM-B3 and the chair of the arbitral tribunal must verify the parties' abidance of the duty of confidentiality (article 6.1), and (iv) the arbitration documents must remain private and non-public.<sup>104</sup>

The downsides of handling corporate and capital markets litigation under a cloak of confidentiality are (i) the asymmetry of information and (ii) the lack of a body of public case law in corporate dispute matters, especially involving listed companies.<sup>105</sup> The confidentiality also represents a relevant barrier for collective redress. The investors may have a total lack of adequate information on the wrongdoing and that will also hinder their ability to join collective suits commenced by others, as further explained below.

### 4.14. Issues for discussion/Recommendations

#### a) Establish legal and contractual (arbitration center) rules governing collective arbitration

Many of the jurisdictions analyzed by Profs. Monteiro and Beneduzi's Chapter do not set forth rules regarding collective arbitration and several of them do not even set forth *class actions/collective suits* rules.

The UK law does not establish legal proceedings such as US-style class actions and collective arbitrations are non-existent (item 3.9 of the current document). In France the class actions were incorporated in the legal system only in 2014 and do not encompass collective disputes between shareholders and the company (item 3.2 of the current document). In Germany, “disputes over rights of minority shareholders of publicly held companies (...) are not arbitrable” and may be adjudicated collectively only by state courts (item 3.3 of the current document).

The Israeli law does provide for class actions and in theory does admit the arbitrability of shareholders disputes, however in practice it is not the common way to resolve collective shareholders disputes. In spite of the well-developed system of derivative claims and class actions in Israel, “arbitration is apparently not the common way to solve shareholder's disputes, at least collectively” (item 3.4 of the current document). Singaporean Law is quite restrictive when it comes to collective redress. The system is mostly based on English Law and does not provide a collective mechanism as seen in US-style class actions (item 3.7 of the current document).

The US law does not contain collective arbitration rules, although some arbitration centers do. Nonetheless, Profs. Monteiro and Beneduzi inform that the chapter “did not identify any cases in practice of class arbitration being used to resolve shareholders’ disputes in the US” (item 3.10 of the current document). This is probably because US case law and the SEC historically have discouraged mandatory arbitration for corporate disputes. In sum, the US does have favorable case law and prepared arbitral institutions to deal with class actions and class arbitration, but apparently the use of class arbitrations for shareholder disputes has not yet been tested in practice.

The analyzed data shows that Brazil has a unique situation: a significant proportion of listed companies have opted to submit their corporate and capital market disputes to arbitration, which furthermore has recently resulted in cases of collective corporate and capital arbitrations, as seen above.

Brazilian law does contain rulings on class actions, but Brazilian law and arbitration centers have yet to set forth specific rules on collective arbitration. Despite this fact, collective corporate and capital market arbitral proceedings have already become a reality in the country with an increase certainly expected in the future. This current trend clearly suggests that Brazil should adopt distinct rules on collective arbitration, as these proceedings have particularities which current bilateral arbitration rules address insufficiently.

How and where to prescribe the rules governing such proceedings are the first questions that would arise when debating collective arbitration. One possible way would be for the arbitration centers to set these rules: arbitration is a contractual dispute resolution mechanism and it would only make sense that the rules should be stated by the parties and the arbitration centers chosen by them.

In fact, none of the jurisdictions analyzed by Profs. Monteiro and Beneduzi’s Chapter set forth *legal rules* on collective arbitration. The only country to specifically determine rules regarding collective arbitration is the US. However, these rules are not provided by the law but by the arbitral institutions, such as the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS (Profs. Monteiro and Beneduzi’s Chapter, item 3.10 of the current document).

Some scholars adopt a hybrid position that the rules should be determined mainly by the arbitration centers and also by the law to a lesser degree.<sup>106</sup> This is the position taken by Profs. Monteiro and Beneduzi:

*“the large use of class arbitrations in the United States — where the Federal Arbitration Act is silent on the subject — suggests that the rules of arbitral institutions such as those from the American Arbitration Association (AAA) and the Judicial Arbitration and Mediation Service (JAMS) are perhaps better suited than statutory provisions to regulate in detail how proceedings in class arbitrations should be carried out because the applicable rules can be more easily changed and adapted when needed while arbitral institutions are also more responsive than lawmakers to the feedback provided by users of the service” (item 3.11 of the current document).*

(...)

*“For the sake of legal certainty, nonetheless, the Brazilian Arbitration Act could be also amended in order to dispel doubts about the legality of this type of agreement under which someone agrees to be bound by an arbitral award rendered in proceedings to which he or she was not a party” (item 3.11 of the current document).*

It appears that the best possible option for Brazil would be the latter, i.e., to leave it to the arbitration centers to set out specific rules on collective arbitration but to also have some rules stated in the law. The law could (i) expressly admit collective arbitration, which would clear up any doubt on its usage, and (ii) provide for *generic guidelines* regarding the procedural safeguards that must be respected by the arbitration centers and then permit them to delimit and specify these rules. This subject still requires further analysis, but these generic guidelines could set forth that (i) collective arbitration is admissible under Brazilian law, (ii) the shareholders and the market must have proper and adequate information about the commencement and the development of the arbitration, (iii) corporate arbitration involving listed companies should be public (non confidential), (iv) the arbitration centers can adopt an opt out system<sup>107</sup> and a specific model of *erga omnes res judicata*, different from the rules set forth in Law 7,347/1985 and in Consumer Protection Code,

that govern court collective suits, if the arbitration centers provide the members of the class with information and certain procedural safeguards. The last suggestion must be thoroughly examined, but in principle it is possible to establish a collective arbitration system that differs from the rules that govern court collective suits. The arbitration centers should have the role to specify these generic guidelines and to establish other rules governing collective arbitrations.

**b) Establish rules making public the information on corporate and capital market disputes involving listed companies**

The confidentiality of the arbitral proceedings makes it difficult for the market – and even for the shareholders of a company involved in the litigation – to have a clear grasp on the aspects surrounding the dispute. This lack of knowledge may end up hindering an informed decision on buying, selling or holding stocks.<sup>108</sup>

The knowledge amassed on corporate wrongdoing and the means of curbing it is of fundamental importance to the application of corporate law and to the development of the capital markets. This knowledge not only reduces the information asymmetries by enabling market participants to engage in adequate pricing of securities and to make a more informed and effective decision but also allows for better monitoring of those involved in the litigation as well as those adjudicating on it.<sup>109</sup>

*Full disclosure* is one of the pillars of the capital market<sup>110</sup> and it is undermined by the confidentiality of arbitration in corporate litigation matters.<sup>111</sup> Confidentiality increases the information asymmetry between market players and even between the shareholders of a same company. This inevitably reduces the efficiency of the capital markets as a whole.

It holds true that listed companies may treat the litigation being referred to arbitration as a *material fact* in that the dispute may have a significant bearing on the trading prices of securities or on the decision to exercise any rights associated with such securities. If arbitration falls under any of such categories, it must be disclosed to the market as provided in article 157, paragraph 4 of the LSA and in CVM Ruling 358. But this disclosure requirement is not enough.

First, not every arbitration would trigger the disclosure of a material fact which is defined by article 2 of CVM Ruling 358 as an event that may have a “substantial” bearing on the securities prices or on the investor’s decisions concerning these securities. The interpretation of what constitutes a material fact is somewhat subjective.

Second, the rules on compulsory disclosure of a material fact do not address its required content which ends up being superficial and poorly detailed. In practice, the material fact touches on the existence of the litigation itself and some of its developments without delving deeply into its content or putting forth supporting documents.

Third, the LSA contains a waiver of disclosure (article 157, paragraph 5) “if the senior management believes that such disclosure may pose a risk to the company’s legitimate interests”<sup>112</sup> which may also help circumvent the disclosure requirements.

When arbitration revolves around a corporate matter or involves the capital market segment, its disclosure is in the interest of *all shareholders* in the company concerned and ultimately of the *market as a whole*. Collective arbitral proceedings should be public with full disclosure<sup>113</sup>, and this especially applies to arbitral proceeding involving corporate disputes that include listed companies. The entire market, and not only the shareholders of the company, should be informed about the dispute and have access to the filings of the proceeding.<sup>114</sup>

A further downside of a confidentiality shield on corporate litigation is that the legal precepts enforceable in this regard are unknown or vague to the public without further details on the concrete application of the rules within the context of the litigation. This is a serious problem in that it impairs the creation of robust *corporate jurisprudence*.

In 2019 the CAM-B3 began publishing a digest of arbitral awards, which is redacted for information on the arbitration proceedings and their parties.<sup>115</sup> This important breakthrough is insufficient for a full understanding of the decisions or the rationale behind them. Apparently, no other Brazilian arbitration chamber to date has published a digest of this type.

According to s. 9 of the American Arbitration Association Supplementary Rules for Class Arbitrations, “the presumption of privacy and confidentiality in arbitration proceedings shall not apply in class arbitrations” and “all class arbitration hearings and filings may be made public”. The institution maintains on its website a “class arbitration docket” with information about the cases, such as copies of some motions, the identities of the parties, the names of the arbitrators, the names of the counsel, copies of the awards (including the final award), and information about any scheduled hearing (date, time and place). There is no confidentiality in collective arbitrations administered by the American Arbitration Association (Profs. Monteiro and Beneduzi’s Report, Chapter 3 of the publication).

This Chapter suggests that arbitrations involving corporate litigation should generally be non-confidential or, at most, the confidentiality treatment accorded to it should be lessened. This position is in line with the conclusions of the Interim Report: “In conclusion, it is clear to the WG that maintaining confidentiality with respect to the course and outcome of arbitral proceedings about corporate and capital markets issues and involving publicly-held companies is not recommended” (Section 3.3.4.3 of the Interim Report).

More specifically, this Chapter suggests that if the litigation of listed companies has an impact on the legal realms of other shareholders and investors (*litisconsórcio unitário*), (i.e., if the award is capable of binding people who are not parties in the arbitration) the whole market should have access to the data and documents surrounding the dispute. When the litigation has no such impact, then the managers, in response to their disclosure duty (article 157, paragraph 4 of the LSA and CVM Ruling CVM 358), should consider whether the arbitration and its procedural acts imply a material fact. If the answer is positive, then such information should be disclosed to the market. Otherwise, no disclosure would be required.<sup>116</sup>

### **c) Establish rules to disclose to the market proper information on the commencement and development of the arbitration**

A fundamental aspect of a collective arbitration system is that the interested parties must be kept informed of the commencement and development of the arbitration. The passing of information to the interested parties is the only possible way to legitimize the proceeding, to make third party intervention feasible and to bind the members of the class to the award (*erga omnes* effect).

This is especially true in litigation involving listed companies, where the information of a collective arbitration involving them is of interest to the entire market. This concern was a subject of the Interim Report:

*“During the workshop, Prof. Dr Christian Borris presented the German experience on the matter – discussed in a context of limited liability companies. In 2009, the German Federal Supreme Court ruled in the case known as ‘Arbitrability II’ that arbitration agreements shall incorporate some features in order to legitimize the erga omnes/res iudicata effects on all shareholders: (i) all shareholders must be bound by the arbitration agreement; (ii) all shareholders have the right and must be given an opportunity to participate in the selection of arbitrators; (iii) all shareholders must be given the opportunity to participate in the arbitration; (iv) parallel arbitrations relating to the same shareholder resolution must be precluded. (...).*

(...)

*Regardless of the mechanisms that will be considered as the most suitable to the Brazilian reality, it is clear to the WG that any participation mechanism will only work properly if there is an adequate disclosure of the proceedings. According to some scholars, while confidentiality can be accepted for certain cases that only affect the parties of the proceeding, it is inadmissible when there are other interested parties that do not or cannot participate in the proceeding. After all, if existing rights common to all or at least a group of shareholders are at stake, the non-disclosure of a case/decision will prevent them from the possibility of co-claiming their*

rights. Therefore, only the most informed and well-assisted shareholders, that filed the arbitration, will have had full access to justice, making clear the social costs associated to this situation.” (Section 3.3.3 of the Interim Report).

In the same direction Profs. Monteiro and Beneduzi’s Chapter states that “shareholders must be given proper and timely notice of the initiation of the arbitration and its subject matter” (item 3.1.4 of this document).

According to the AAA Supplementary Rules for Class Arbitrations, in the initial phase of the arbitration, the arbitral tribunal must render a partial award defining the class, the class representative, the class counsel as well as the class claims, issues and defenses. This decision is called “class determination award” and must be notified to all members of the class by “the best notice practicable under the circumstances” (s. 6)<sup>117</sup>. Once the notice is given the members of the class have the faculty to opt-out of the class arbitration and pursue their claims individually, “otherwise they will be bound by the future arbitral award, as set forth in Rule 6(b)(6)”<sup>118</sup>. JAMS Rules also state a similar rule (s. 4(6))<sup>119</sup>. The German *Bundesgerichtshof* (BGH) has also ruled that in arbitrations involving limited liability companies the shareholders must be granted “a fair opportunity to participate in the proceedings in general and in the constitution of the tribunal in particular”.<sup>120</sup>

For the same reason disclosing information to the market is crucial for an effective opt out collective system of redress. The “shareholders must have the right to opt out from the arbitration if they so wish”.<sup>121</sup> And to make that possible the shareholders must be appropriately informed on the beginning and the development of the arbitration. Information is the key to legitimating the proceeding and making feasible *erga omnes* effects.

Full disclosure of the arbitration is a fundamental aspect to legitimize the process and the information could be provided to the shareholders and investors in various forms: (i) personal notification, (ii) filing of the request for arbitration with the trade boards<sup>122</sup>, or (iii) publication on the internet.

Publishing the information, data and documents of the arbitration on the internet appears to be the most adequate and least costly way to provide full and effective disclosure. Brazil should consider adopting rules that set forth the duty of the company to properly inform the shareholders and the market on the initiation as well as the development of the proceeding. The author considers that the internet is the best locus as it is the least expensive and most effective way to ensure that the shareholders will obtain the information.

#### **d) Establish rules regarding third party intervention**

Another problem of adopting arbitration to resolve corporate disputes of publicly held companies relates to the difficulties concerning the intervention of third parties. In disputes marked by a unitary nature, the possibility of such intervention is an essential tool for validating the award and its *erga omnes* effects, as it enables the interested parties to express themselves and participate in the process which will result in an award that affects them as well.<sup>123</sup>

These difficulties arise, above all, from confidentiality: if the third party does not have access to the particulars of the dispute and, in some cases, does not even know it exists, it cannot make an informed decision as to whether it should intervene in the arbitration proceeding. In arbitration the third party faces an additional difficulty, which is the knowledge of the existence of the arbitral proceeding and, most of all, the subject matter in dispute.

In other words, lack of proper information is the first obstacle for third parties to intervene in pending arbitral proceedings. It is worthless to set forth rules condoning voluntary third-party intervention if there is a lack of adequate information for the third party to make a decision on its intervention.<sup>124</sup>

Making third party intervention possible is essential to legitimize the proceedings that may bind those other than the parties. That is the very reason why article 2.1 of Annex 5 of the Deutsche Institution für Schiedsgerichtsbarkeit (DIS) Rules of 2018 establishes that “*in disputes requiring a uniform decision*

*binding all shareholders and the corporation, and in which a party intends to extend the effects of an arbitral award to any shareholder or the corporation who are not named parties to the arbitration ('Concerned Others'), the Concerned Others shall be granted the opportunity to join the arbitration pursuant to these DIS-CDR as a party or compulsory intervenor in the sense of Section 69 of the German Code of Civil Procedure ('Intervenor')*" (Profs. Monteiro and Beneduzi's Report, Chapter 3 of the publication).

In Portugal the Associação Portuguesa de Arbitragem (Portuguese Arbitration Association) drafted a bill of law and arbitration rules proposals regarding corporate arbitration in 2016. The arbitration rules proposals suggest similar provisions, stating that if the arbitral decision is capable of binding those who are not formal parties to the arbitration, the claimant must list all potentially affected parties, who will be notified of the case and have the right to intervene.<sup>125</sup>

S. 9(2) of the rules of arbitration of the *Corte de Arbitraje de Madrid* states that the arbitrators may, at the request of any party and after hearing them all, admit the intervention of a third party. S. 13 of the CIMA Rules contains a similar provision. However, the problem with these provisions is that third parties may not intervene if not invited by one of the parties to the proceedings, as explained in Profs. Monteiro and Beneduzi's Chapter, item 3.8 of the current document.

Moreover, in different countries, including Brazil, usually the intervention of third parties is generally accepted up until the constitution of the arbitral tribunal.<sup>126</sup> For instance, the CAM-B3 rules set forth the conditions in which the parties of the arbitration may request the inclusion of a third party and the conditions in which a third party may claim to intervene in the proceeding. Third party intervention is allowed only up to the appointment of the arbitrators.<sup>127</sup>

The Italian Law establishes that the forms of third party intervention referred to in the Code of Civil Procedure for court proceedings are also applicable to arbitral proceedings, although only if the arbitrators and all the parties agree (art. 816-*quinquies* of the Italian Code of Civil Procedure). The German Annex 5 of the *Deutsche Institution für Schiedsgerichtsbarkeit* (DIS) Rules of 2018 also applies to arbitral proceedings certain rules of the German Civil Code of Civil Procedure governing the intervention of third parties (Profs. Monteiro and Beneduzi's Report, Chapter 3 of the publication).

Nonetheless, to simply apply the third-party intervention modalities set forth in the codes of civil procedure to arbitration may not be the best approach. Court and arbitral proceedings have differences and peculiarities which supports the conclusion that the indiscriminate transposition of court rules to the arbitral environment may be inadequate. The arbitration centers undoubtedly should learn from the experience of the courts but must also set forth rules taking into consideration the peculiarities of the arbitral proceedings.

All told, rules on third party intervention are fundamental for a collective arbitration system. These rules should set out who may intervene, in what manner and at which stage of the proceeding. The question that arises is *which rules* to prescribe. This Chapter does not have all the answers to that question, but can provide some partial conclusions: (i) disclosing proper information to the interested parties is essential to any third party intervention mechanism; (ii) the indiscriminate transposition of the Brazilian Code of Civil Procedure to the arbitral proceedings is not the best option, as the latter presents peculiarities that must be addressed<sup>128</sup>; (iii) third party intervention is usually accepted until the constitution of the arbitral tribunal, and this rule seems advisable in order to stabilize the arbitration; and (iv) the third parties should not only be summoned to join the arbitration, but also must be granted the opportunity to voluntarily do so.

It is also worth mentioning that the Brazilian law provides that the Public Prosecutors Office must be summoned in judicial proceedings as a law enforcement authority when the case discusses certain aspects. If the collective arbitration involves one of these matters, then the Public Prosecutors Office must also be informed on the arbitral proceeding to intervene if it so desires.<sup>129</sup> The CVM can also serve as *amicus curiae* in arbitral and judicial proceedings regarding matters included under its authority, pursuant to article 31 of Law No. 6,385/1976. This subject will be further addressed below.



### e) Establish rules regarding the constitution of the arbitral tribunal

Party autonomy is the guiding principle of arbitration and for such reason the parties have the prerogative of choosing the arbitral tribunal,<sup>130</sup> as well as appointing and defining the number of arbitrators.

Under Brazilian law the arbitral tribunal must comprise an odd number of members; if an even number of members is appointed, such members must appoint another arbitrator (Arbitration Act article 13, paragraphs 1, 2 and 4).<sup>131</sup> In practice, as a rule, arbitral tribunals are composed of three arbitrators, since the risk of error is reduced when the parties appoint more than one arbitrator.<sup>132</sup> Therefore, each party (or the parties on each side of the dispute) appoints one arbitrator, and these two arbitrators appoint the chairman of the tribunal.

In multiparty arbitration problems may arise when the arbitral tribunal is constituted, as the rule which establishes that each party must appoint an arbitrator only works properly in arbitrations involving two sides of interest or in those in which, although there are more than two sides, the parties on each side have similar interests. This general rule does not apply when there are several different sides with different interests, as may happen in a dispute involving shareholders of a company and the company itself, which, in a given dispute, may have opposing interests.<sup>133</sup>

Multiparty arbitrations usually adopt two solutions when deliberating arbitral tribunal constitution. The first possibility is to set a deadline for the plaintiffs and the defendants to indicate one arbitrator each. If either party fails to reach a consensus on its indication, all the members of the arbitral tribunal or at least the co-arbitrators should be selected by the arbitral institution. Otherwise, the only feasible alternative is to confer on an impartial third party (perhaps the arbitration body itself, in the event of institutional arbitration) the task of appointing the arbitrators. Therefore, the second possibility is to eliminate that phase and go directly to indications by the arbitral institution or another third party.<sup>134</sup>

Italian law expressly prohibits the articles of association of listed companies to contain arbitration clauses (*Decreto Legislativo* n. 5 of 17 January 2003) but it does admit corporate arbitration involving non listed companies. The law states that the tribunal in corporate arbitration is to be appointed by a person or institution outside the company. More specifically, the rules set out that the arbitration agreement must expressly indicate a third party, with no relationship to the company, which will have the duty to nominate the arbitrators. If the arbitration agreement does not contain such rule the arbitrators must be nominated by the president of the judicial court in which the company is headquartered (*Decreto Legislativo* n. 5 of 17 January 2003 Article 34, paragraph 2) (Profs. Monteiro and Beneduzi's Report, Chapter 3 of the publication).

As mentioned before, the Associação Portuguesa de Arbitragem (Portuguese Arbitration Association) drafted a bill of law and arbitration rules proposals regarding corporate arbitration in 2016. One proposes that the arbitral institution appoints the sole arbitrator or all the members of the arbitral tribunal in corporate arbitrations (s(4)(4))<sup>135</sup>. The other suggests that the arbitral institution appoint the arbitrators, except in cases where the parties had already agreed on the names. If the parties cannot reach a consensus, a sole arbitrator or whole arbitral tribunal would be appointed by the arbitration center (s. (5)(2); Profs. Monteiro and Beneduzi's Report, Chapter 3 of the publication). Additionally, in cases of relief for the annulment of shareholders resolutions or if the award may bind formal non-parties to the arbitration, the agreement on names is irrelevant as the arbitration center will appoint the sole arbitrator or the arbitral tribunal.<sup>136</sup>

In the US the AAA Supplementary Rules for Class Arbitrations state that (i) the arbitral institution has a specific list of arbitrators who are specialists in class arbitration, and (ii) the arbitral institution will appoint at least one of the arbitrators (in general, the presiding arbitrator) (Profs. Monteiro and Beneduzi's Report, Chapter 3 of the publication).

Taking account of all these possibilities, the best solution is to give the parties the opportunity to reach a consensus on the appointment of the co-arbitrators and subsequently the arbitrators appoint the president of the tribunal. The ability to choose and appoint the arbitrators is one of the main advantages of arbitration.

Therefore, the parties should be afforded this possibility even in collective arbitrations. If the parties do not reach a consensus after a specific time established by the arbitration center, then the arbitration center will appoint the sole arbitrator or the co-arbitrators. In the last situation, the president of the tribunal must be appointed by the co-arbitrators.

If the intervention of a third party is admissible after the appointment of the arbitrators, then it must accept the composition of the arbitral tribunal as prescribed by S. 52(5) of the rules of arbitration of the *Corte de Arbitraje de Madrid* and by s.68((5) of the rules of the *Centro de Arbitraje Internacional de Madrid (CIAM)*.

#### **f) Discuss establishing specific rules on allocation of costs in collective arbitration**

Compared to court litigation arbitration is more costly,<sup>137</sup> as the parties incur expenses with arbitrators as well as the managing body fees. Although, some argue that if one considers all transaction costs involved in a judicial proceeding – delay, uncertainty, lack of legal certainty –, court litigation can end up being much more costly.<sup>138</sup>

There are some alternatives to bring down such costs. The parties may choose to submit the dispute to a sole arbitrator<sup>139</sup> and reduce costs of arbitrator fees, which represent a significant expense in an arbitral proceeding. They may also opt for an arbitration chamber that is less expensive than the average or even for arbitration *ad hoc*, which entrusts management of the case to an arbitration body.

Even employing the expense-reducing techniques above arbitration is still costly, at least when comparing direct and immediate expenses. This discourages parties from resolving their corporate disputes through arbitration. Listed companies may have tens or hundreds of millions of small investors and quite often their investment is less than the average spent with merely the initial arbitrators' fees.<sup>140</sup> It is very unlikely the individual investor would be adversely affected by a shareholders' resolution or by an act of management that will initiate arbitral proceedings alone. From a cost perspective this may indicate that arbitration is making the enforcement of corporate and Brazilian capital market rules more daunting and is discouraging small investors instead of stimulating them to exercise their rights. For such reason it is necessary to consider mechanisms that reduce arbitration costs and facilitate access to justice within the arbitration sphere. Accessibility to arbitration by the average investor is essential and corporate disputes costs involving listed companies must be affordable for the investor.

This Chapter has analyzed the cost of the proceedings and attorney fees aspects in derivative lawsuits. Article 27 of the Brazilian Arbitration Act establishes that “the arbitral award shall decide on the parties' duties regarding costs and expenses for the arbitration, as well as on any amount resulting from bad faith conduct, if applicable, complying with the provisions of the arbitration agreement, if any”, but sets forth no criteria for such division. Therefore, the parties are free to stipulate how the costs of the proceeding will be shared at the end of the arbitration. Usually the arbitral agreements and the arbitration center rules set forth that the losing party must reimburse the winning party for the costs of the litigation (arbitrators fees, chamber fees, expert fees etc.), except for the attorney fees. As explained previously in this chapter, the CPC “loser pays” rule does not necessarily apply to arbitration proceedings as the CPC is not automatically applicable to arbitrations. The rule will only govern arbitral proceedings if the arbitration convention stipulates so and, thus, the arbitral tribunal has no authority to award loss-of-suit fees unless stipulated by the parties.

The assessment and the conclusions that have been made in that section are applicable to arbitral proceedings involving those claims, which are usually bilateral disputes. Remaining is the question on whether there should be *specific rules* on allocation of costs for collective arbitration.

Chapter 3 suggests that “arbitral institutions and regulators could establish special rules concerning allocation of costs in securities matters — diverging from those applicable to securities litigation before state courts — so that they may serve as an economic incentive for shareholders to seek redress on their behalf and, even more importantly from a regulatory point of view, on behalf of the company” (See Section 3.11.6).

However, the jurisdictions analysed for this review lacked specific rules on the allocation of costs. The only special provision on the matter can be found in the AAA Supplementary Rules for Class Arbitrations, which, as explained in the chapter, set forth that “the claimant is required to pay USD 3 350 (a ‘preliminary filing fee’) to file a claim, counterclaim or additional claim as a class arbitration. These initial fees will cover all arbitral institution fees until the rendering of the ‘clause construction award’. In case of a favourable decision, accepting the availability of the class arbitration, a supplemental filing fee – calculated on the basis of the amount in dispute – is required from the claimant. If one of the parties fails to pay the costs, the other one will be notified to pay the amount required”.

This Chapter is of the opinion that the arbitration centers should prescribe specific allocation of costs rules in collective arbitration. However, the experiences of other countries suggest that perhaps corporate and collective arbitration should be governed by the general rules applicable to all arbitrations. This Chapter does not have a final conclusion on this subject.

### **g) Discuss establishing rules on adequacy of representation**

The Brazilian law does not expressly provide for a court control of adequacy of representation in collective suits. This procedure is contemplated neither in the Law 7,347/1985 nor in the Consumer Protection Code (which applies to all collective suits, and not only to consumer disputes). This fact has led some legal scholars to state that such control has been previously done by the law (*ope legis* control), which means that it should be presumed that the legal entities listed in article 82 of the Consumer Protection Code are adequate representatives to file a public civil action (*ações civis públicas*).<sup>141</sup>

However, based on an interpretation of the Brazilian Constitution, some jurists have taken the stand, stating that the Brazilian system of collective relief does not preclude court review of adequacy of representation, despite the absence of an express legal provision.<sup>142</sup>

By means of this interpretation, the Brazilian law indeed admits judicial review of adequacy of representation. Adequate representation is in line with the dictates of due process of law and grants legitimacy and effectiveness to the proceeding.<sup>143</sup> Therefore, the judge must first confirm whether there is legal standing for the plaintiff to act on behalf of the class and to conduct the proceeding. After such analysis the judge must actually review the representation by ruling whether the representative party has a relation to the matters being discussed in the proceeding (*pertinência temática*),<sup>144</sup> whether the representative party has the financial ability to bear the costs of the proceeding, whether its attorneys have the competence and expertise to act, and whether there are any conflicts of interest between the representative, its attorneys and the subject matter of the suit.

The same control should be carried out for in collective arbitration: such proceedings should be subject to an *adequacy of representation* analysis based on the criteria mentioned above, such as knowledge and past experience on the subjects under discussion (of the party and of its counsel), financial ability to bear the costs of the proceeding and absence of conflict of interests, among others.

Pursuant to AAA and JAMS rules on collective arbitration, one of the most important steps of the proceeding is the *class certification*, in which the arbitral tribunal issues a “class determination award”, which defines the class, as well as its representative and counsel, among other issues (s. 5 of the AAA Rules and s. 3 of the JAMS Rules). The class members must be notified of the decision and have the opportunity to opt out of the arbitration. If they do not wish to be bound by the final award, they may opt out and pursue their claims individually.

When issuing a class determination award and defining the representative parties and the counsel that will represent the class, the arbitral tribunal must consider any law or agreement applicable and assess if “the representative parties will fairly and adequately protect the interests of the class” (s. 4(a)(4) of the AAA Rules) and if “the counsel selected to represent the class will fairly and adequately protect the interests of the class” (s. 4.(b)5).

Similarly, s. 3(a) of the JAMS Rules sets out that when certifying the class the arbitrator “shall determine whether one or more members of a class may act in the arbitration as representative parties on behalf of all members of the class described” and that “shall permit a class member to serve as a representative only if the conditions set forth in the Federal Rules of Civil Procedure, Rule 23(a), are met”.<sup>145</sup>

Rule 23(a) of the US Federal Rules of Civil Procedure establishes that one or more members of a class may sue or be sued as representative parties on behalf of all members if certain prerequisites are met, including “if the representative parties will *fairly and adequately protect* the interests of the class” (Rule 23(a)(4)).<sup>146</sup>

The choice of class counsel is set forth in Rule 23(g), which establishes that the court that certifies a class must appoint the class counsel, considering different criteria such as (i) the work the counsel has done in identifying or investigating claims in the action, (ii) counsel’s track record regarding class actions, complex litigation and the subjects discussed in the proceeding, (iii) counsel’s knowledge of the law, (iv) the resources that counsel will commit to representing the class and (v) any other matter pertinent to counsel’s ability to fairly and adequately represent the interests of the class.<sup>147</sup>

The Private Securities Litigation Reform Act (PSLRA) of 1995 amended the Securities Exchange Act (which is codified in [Section 78 of Title 15 of](#) the U.S. Code) and established the rebuttable presumption that in certain securities class actions, the most adequate representative is the party that “has the largest financial interest in the relief sought by the class”, since it is, in theory, the party with the greatest incentive to defend the common interest (15 U.S.C. 78u-4(a)(3)(b)(iii)).<sup>148</sup>

By doing so the law intends to align interests and, consequently, reduce agency costs and attorneys’ power over the suit. This is a rebuttable presumption that the member most harmed by the wrongful act is, as a rule, the party most qualified to act as a class representative. The class representative may choose its own counsel under the judge’s supervision (15 U.S.C. 78u-4(a)(3)(b)(v)).<sup>149-150</sup>

This criterion should be regarded with some reservations. Brazil could indeed adopt it, but as *one among* several other reference criteria. The majority shareholder is not always aligned with the interests of the company or of the other shareholders. Moreover, adoption of this criterion on an absolute basis would entail additional problems in state-controlled companies.

In sum, one should consider establishing a control of adequacy of representation in collective arbitration, taking into account different criteria such as (i) party’s and counsel’s previous experience regarding collective arbitration and the matters under discussion, (ii) potential conflicts of interest, (iii) financial capacity and (iv) other criteria that indicate that the party and its counsel will be able to fairly represent the class.

#### **h) Establish rules prescribing terms and conditions for third party funding**

Litigation is expensive and for such reason issues related to procedural costs may hinder access to justice.

An alternative to overcome these difficulties is to seek third-party funding (by investment funds and specialized companies), as happened initially in Australia and subsequently in other countries such as the United Kingdom, Canada and South Africa. This alternative has become increasingly widespread in other countries, including Brazil.<sup>151</sup> According to Profs. Monteiro and Beneduzi, Israeli courts are opposed to private entity third party funding in class actions.<sup>152</sup>

Funding terms are usually established in a funding agreement, which provides for the obligation to refund and remunerate the investor upon receipt of the credit by the funded party. In the event of defeat, the investor may receive nothing. It is for this very reason such funding is usually preceded by a careful assessment of the chances of success of the party seeking third-party funding.<sup>153</sup>

Third-party funding in Brazil is still quite recent but is increasingly becoming a known and adopted alternative in arbitrations. This fact has led an important arbitration and mediation center to issue a

resolution recommending that, whenever applicable, the parties immediately notify it of the existence of third-party funding. In such notice the funded party must fully identify the funder for verification by the appointed arbitrators for any conflicts of interest and, being the case, disclosure of the facts which may give rise to doubts as to the impartiality or independence of one or more members of the arbitral tribunal.<sup>154</sup>

Although this practice is still incipient in Brazil, there is no legal obstacle to third-party funding of court litigation or arbitral proceedings.<sup>155</sup>

Third-party funding also brings with it some concerns, such as the possibility of judges or arbitrators being influenced by the prior assessment made by the potential investor and the possibility of the third-party funder exercising certain influence on the proceeding, even if indirectly, given its interest in the success of the funded party.

These issues should be discussed and properly regulated. However, third-party funding should be allowed as a tool to overcome the hurdles to exercise the right of access to justice and to make possible disputes which would be extremely costly to the weakest party, to the point of discouraging it from filing the suit.<sup>156</sup>

The arbitration centers should consider rules expressly accepting third party funding and establishing the terms and conditions for it, including for the disclosure and management of potential conflicts of interest. This would reduce the uncertainties involved in the third party funding as well as foster it. This suggestion is in harmony with the conclusions of the Interim Report:

*“Although not studied in detail for this report, another possibility that can allow compensation would be the involvement of third parties, either (i) to finance the litigation (scholars have been studying the feasibility of third-party funding in arbitral proceedings); or (ii) to replace the shareholders in the litigation through the transference of “litigation rights” (e.g. compensation rights sought in arbitrations) to third-parties interested in seeking their rights<sup>78</sup> (see Article 109 of the Brazilian Civil Procedure Code). Both ideas were mentioned during the Workshop by panelists and, at a first glance, appear to be possible means to address the problems of costs and redress.” (Section 3.3.2 of the Interim Report).*

**i) Consider expressly stating that the CVM must be called to intervene as *amicus curiae* in capital market disputes arbitration and not only in judicial proceedings**

One way of overcoming the Judiciary’s lack of expertise in corporate and capital market matters is to have the CVM serving as *amicus curiae* in judicial proceedings. This role is set out in article 31 of Law No. 6,385/1976: “In any judicial proceedings or actions regarding matters included under the authority of The Securities Commission of Brazil, the latter shall always be notified and be given the opportunity to submit an opinion or render explanations within a period of fifteen days of the date of the notice”.

Under this legal provision – which was the first provision to introduce the “friend of the court” mechanism into the Brazilian legal system – the judge has the duty<sup>157</sup> to invite the CVM to offer information or advice on “lawsuits involving matters within its sphere of authority” should the CVM find it suitable.<sup>158</sup> It is important to note that the CVM will only intervene if it finds adequate, as properly explained in the Interim Report:

*“taking into account all the functions assigned to CVM, it understands that it must exercise the legal prerogative to act as “amicus curiae” only in exceptional situations which, in addition to falling within its competence, involve matters with relevant repercussions to the capital markets or to a relevant part of its participants” (Section 2.2 of the Interim Report).*

The rationale behind this rule is clear: given the specificities of capital markets litigation, the CVM should be called upon to provide insight on questions of law or fact<sup>159</sup> thereby assisting the judge to render a seasoned decision on the matter in dispute.<sup>160 161</sup>

The CPC also provides for *amicus curiae* as a type of third-party intervention.<sup>162</sup> CPC article 138 reads that, considering the relevance of the matter at issue, its specificities or the social repercussions of a dispute, the judge may – based on a non-appealable decision, on his own initiative or at the request of any litigant or of an interested third person – order or permit a third individual, body or entity (with adequate representation powers) to act as *amicus* within 15 days of the notice date.<sup>163</sup>

The CVM role as *amicus curiae* in cases surrounding matters that fall within its sphere of institutional authority is an interesting way to bring public and private aspects together for legislative enforcement purposes. This aspect drove Prof. John Coffee Jr. to suggest that the regulatory body should provide advice and oversight in those settlements by acting as *amicus*<sup>164</sup> to rule out potential conflicts of interests and the risk of collusion in settlements for collective suits involving capital market disputes in the USA.

Article 31 of Law No. 6,385/1976 suggests that the CVM should intervene only in court disputes, which would in principle rule out its role as *amicus* in arbitration. This is not the best interpretation though. The aforementioned article makes no express reference to arbitration because when the provision was enacted this alternative dispute resolution mechanism did not exist as it is today in 2020. For this same reason, calling in the CVM to offer insight or advice in court disputes should also extend to arbitration. If the law requires the CVM to assist in financial markets disputes, this should also hold true for arbitration involving matters within its authority.

Some experts advocate that, as the CVM is a federal independent government agency, its participation as *amicus curiae* vests the federal court with legal authority to adjudicate on the corresponding dispute.<sup>165</sup> This is technically questionable in that the ‘friend of the court’ is not a party acting in defense or support of claims of its own.<sup>166</sup> This stand is also questionable in terms of convenience as only state courts have corporate chambers and district courts. Nonetheless, since the enactment of the CPC in 2015, there clearly must be no change of jurisdiction (as expressly stated in its article 138, paragraph 1).

Based on the above, perhaps the Brazilian law should be clarified to ensure that the CVM is notified to offer information or advice on arbitration “involving matters within its sphere of authority” should the CVM find it advisable, and not only on court disputes.<sup>167</sup> The collective arbitration involving capital market and corporate disputes of listed companies would fit in this rule. This amendment is necessary to clarify the existing legal rule (article 31 of Law No. 6,385/1976).

#### 4.15. Conclusions

This chapter analyses various aspects of derivative suits and collective arbitration systems, reaches conclusions and makes recommendations for Brazil regarding these issues. These conclusions and recommendations are explained and justified in detail in the previous sections of the chapter. To facilitate the understanding, the two following tables bring together and summarize the main aspects of this chapter. However, we strongly advise the reader to go through the entire chapter, as the tables merely summarize the conclusions and recommendations without explaining the rationales on which they are based.

Table 4.2. Proposals on derivative suits

Number	Proposals on derivative suits
1	<u>Eliminate</u> or <u>modify</u> the rule that exonerates the managers from liability ( <i>quitus</i> ) upon approval of financial statements and management accounts (LSA article 134, paragraph 3), to read that only the facts expressly reported to the shareholders at the general meeting or by the official communication of the company would have exonerating effects.
2	<u>Consider</u> establishing a pre-trial/screening lawsuit admission procedure to decide on the acceptance of derivative suits, to (i) eliminate abusive claims and permits the meritorious to move forward and (ii) to limit the exposure of the plaintiff to financial litigation risk.
3	<u>Consider</u> eliminating or modifying the rule that demands the prior shareholders meeting to pursue liability against managers (LSA article 159) This rule is not in line with most of the jurisdictions analyzed by Prof. Gelter. In Brazil the potential plaintiff should have the <i>option</i> to submit the claim to the shareholder meeting to obtain certain effects, such as the disqualification of the defendant manager (LSA article 159, paragraph 2). But submitting the matter to the shareholder meeting would be an option and not a <i>necessary requirement</i> .
4	<u>Establish</u> that any controlling shareholder can be the defendant in the lawsuit set out in LSA article 246: a company, an individual or any other entity (e.g., an investment fund). This modification is necessary because LSA article 246 <b>states that “the controlling company will be required to redress the damage (...)”, which may be construed as only</b> a controlling <i>company</i> can be sued for damages. The law should clarify that the suit for damages can be brought against any kind of controlling shareholder to avoid misinterpretation.
5	<u>Clarify</u> that the lawsuit set out in LSA article 246 is not subject to the provisions outlined in LSA article 159 and no previous resolution at a general meeting is needed to file the suit. LSA article 246 does not refer whatsoever to a general meeting resolution, which leads to the conclusion that such requirement has no legal grounds. But it is advisable that the law expressly state such position considering some court rulings have adopted a different interpretation.
6	<u>Unify</u> the systems for reimbursement of expenses for the lawsuits brought under LSA articles 159 and 246. The two claims should have been afforded the same provisions as they all lead to the same: a shareholder acting as nominal plaintiff of the company seeking payment for damages that will ultimately accrue to the company if successful. They should be governed by the same provisions – preferably those set out in LSA article 159, paragraph 5 which is more comprehensive by determining the reimbursement of <i>all reasonable expenses</i> incurred with the case including interest and adjustment for inflation.
7	<u>Modify</u> the rule set out in LSA article 159, paragraph 3, to establish that when a shareholder brings a suit on account <b>of the company’s unresponsiveness the latter must bear all costs of litigation regardless of its outcome</b> . There should be full reimbursement of the costs in the event of LSA article 159, paragraph 3, when the general shareholders meeting has adopted the filing of a suit (resolution to sue) but the management has failed to comply. The company should reimburse the costs regardless of the outcome of the suit in these cases. If the Brazilian law adopts a preliminary procedure for the admission of derivative suits, as discussed in item 2.1.2.(b) of this Chapter, the reimbursement by the company of the reasonable litigation costs should also be considered if the plaintiff is successful in a preliminary stage.
8	<u>Extend</u> the attorney fees and bonus payment provisions under LSA article 246 to the lawsuit laid out in LSA article 159. The 5% bonus and the 20% attorney fees set out in LSA article 246 are justifiable not only in the context of lawsuits brought against the controlling shareholder but also for those against the managers.
9	<u>Expressly state</u> that the 20% attorney fees and the 5% bonus accrue on the <i>total amount of the award</i> and not only on the amount that is proportionate to the ownership of the shareholder. Contrary to what LSA article 246, paragraph 2 <sup>o</sup> establishes, some court rulings have ruled that the 5% bonus and the 20% attorney fees should be calculated not on the total amount of the award but <b>rather on the plaintiff shareholder’s ownership percentage</b> multiplied by the amount of the award. This amendment is necessary to clarify the existing legal rule and to eliminate those interpretations.

Number	Proposals on derivative suits
10	<p><u>Consider</u> modifying the “loser pays” rule to foster derivative suits. The “loser pays” rule discourages frivolous litigation but also deters shareholders from filing lawsuits as representatives of the company. Perhaps the rule should be addressed to foster derivative litigation in the Brazilian capital market. If the Brazilian law adopted a preliminary procedure to decide on the admission of derivative suits and if the claim is cleared as discussed in item 2.1.2.(b) of this Chapter, then the reimbursement of the reasonable litigation costs by the company, including attorney fees, should also be considered. A second possible solution would be to cap the attorney fees for unsuccessful derivative lawsuits. The third possibility would be to exempt the plaintiff from paying attorney fees except in case of bad-faith or frivolous claims. This rule would be similar to articles 17 and 18 of Law 7,347/1985 which states that if an association initiates a class action (<i>ação civil pública</i>) and the case is dismissed the plaintiff must not be condemned to pay attorney fees and other costs of the proceedings except in case of bad faith.</p>
11	<p><u>Modify</u> the law to give the CVM greater leeway to change the percentage ownership interests set out in LSA article 291 by considering criteria other than the capital stock. Criteria better <b>reflecting a company's ownership dispersion</b> should be included in LSA article 291 for a reduction in the threshold percentages. It would be advisable that LSA article 291 gave the CVM some leeway to reduce the threshold percentages after considering the capital stock but also other factors, such as extent of stock dispersion, the existence of a defined controlling entity, to name a few.</p>
12	<p><u>Consider</u> establishing rules regarding contemporaneous and continuous ownership of stock. There is no requirement under Brazilian law on contemporaneous and continuous ownership of stock of the harmed company at the time when the wrongdoing was committed or when the court decision is rendered. We face two central questions in relation to the issue: (i) whether the law should require contemporaneous and continuous ownership of stock of the harmed company at the time when the wrongdoing until the court decision is rendered; (ii) in either case, if the law should be amended in order to clarify which rule applies in Brazil.</p>
13	<p><u>Consider</u> establishing rules regarding subsequent control over a derivative suit and settlements. The LSA does not have any provision regarding the requirements for settling or waiving a derivative claim. Perhaps the Brazilian lawmakers should consider establishing a rule demanding that settlements must be approved by the court or by the shareholders, which could also include granting minority shareholders the right to veto the decision.</p>
14	<p><u>Consider</u> establishing evidence production mechanisms in order to reduce the information asymmetry among shareholders, the company, the controlling shareholders and the managers. The best way to provide the shareholder with information and at the same time to prevent <i>discovery abuse</i> is to grant the plaintiff with reasonable production of evidence under supervision of the court or the arbitral tribunal, provided that the plaintiff shows preliminary evidence of the wrongdoing and proves that has tried to obtain the documents before requesting the judicial or arbitral order. In other words, the shareholder should be granted a broader access to evidence if it presents <i>prima facie</i> evidence of the facts that justify the derivative suite. We should also consider the shift in the burden of proof, pursuant to article 373 of the CPC.</p>



Table 4.3. Proposals on collective arbitration

Number	Proposals on collective arbitration
15	<u>Establish</u> legal and contractual (arbitration center) rules governing collective arbitration. Taking into consideration the experience of other countries it appears that the best possible option would be to leave it to the arbitration centers to set out specific rules on collective arbitration but to also have some rules stated in the law. The Brazilian law could (i) expressly admit collective arbitration, which would clear up any doubt on its usage, and (ii) provide for only <i>generic guidelines</i> regarding the procedural safeguards that must be respected by the arbitration centers. The arbitration centers themselves would be entitled to delimitate and specify these rules.
16	<u>Establish</u> rules making public the information on corporate and capital market disputes involving listed companies. Arbitrations involving corporate litigation should generally be non-confidential. This Chapter suggests that if the litigation of listed companies has an impact on the legal realms of other shareholders and investors ( <i>litisconsórcio unitário</i> ), i.e., if the award is capable of binding people who are not parties in the arbitration, the whole market should have access to the data and documents surrounding the dispute. When the litigation has no such impact then the managers, in response to their disclosure duty (article 157, paragraph 4 of the LSA and CVM Ruling CVM 358), should consider whether the arbitration and its procedural acts characterize a material fact. If the answer is positive, then such state of affairs should be disclosed to the market. Otherwise no disclosure would be required.
17	<u>Establish</u> rules to disclose to the market proper information about the commencement and development of the arbitration. Full disclosure is a fundamental aspect to legitimize the arbitral proceeding. Publishing the information, data and documents of the arbitration on the internet appears to be the most adequate and least costly way to provide full and effective disclosure. Brazil should consider adopting rules that set forth the duty of the company to properly inform the shareholders and the market on the initiation as well as the development of the proceeding. This Chapter believes that the internet is the best locus as it is the least expensive and most effective way to ensure that the shareholders will obtain the information.
18	<u>Consider</u> establishing a control of adequacy of representation in collective arbitration, taking into <b>account different criteria such as (i) party's and counsel's previous experience regarding collective arbitration and the matters under discussion, (ii) potential conflicts of interest, (iii) financial capacity and (iv) other criteria that indicate that the party and its counsel will be able to fairly represent the class.</b>
19	<u>Establish</u> rules regarding third party intervention. Rules establishing who may intervene, in what manner and at which stage of the proceeding are fundamental for a collective arbitration system. The question that arises is <i>which rules</i> to prescribe. This Chapter does not have all the answers to that question, but can provide some partial conclusions: (i) disclosing proper information to the interested parties is essential to any third party intervention mechanism; (ii) the indiscriminate transposition of the Brazilian Code of Civil Procedure to the arbitral proceedings is not the best option, as the latter presents peculiarities that must be addressed; (iii) third party intervention is usually accepted until the constitution of the arbitral tribunal, and this rule seems advisable in order to stabilize the arbitration; and (iv) the third parties should not only be summoned to join the arbitration, but also must be granted the opportunity to voluntarily do so.
20	<u>Establish</u> rules regarding the constitution of the arbitral tribunal. The parties should have the opportunity to reach a consensus on the appointment of the co-arbitrators and subsequently the arbitrators appoint the president of the tribunal. If the parties do not reach a consensus after a specific time, then the arbitration center should appoint the sole arbitrator or the co-arbitrators, and the president of the tribunal must be appointed by the co-arbitrators. If the intervention of a third party is admissible after the appointment of the arbitrators, then it must accept the composition of the tribunal.
21	<u>Consider</u> establishing specific allocation of costs rules in collective arbitration. This Chapter believes that the arbitration centers should prescribe specific allocation of costs rules in collective arbitration. However, the experiences of other countries suggest that perhaps corporate and collective arbitration should be governed by the general rules applicable to all arbitrations. This Chapter does not have a final conclusion on this subject and recommends its discussion in the OECD workshop.
22	<u>Establish</u> rules prescribing terms and conditions for third party funding. The arbitration centers should consider rules expressly accepting third party funding and establishing the conditions for it. This would reduce the uncertainties involved in the third party funding as well as foster it.
23	<u>Consider</u> expressly stating that the CVM must be called to intervene as <i>amicus curiae</i> in capital market disputes arbitration and not only in judicial proceedings (article 31 of Law No. 6,385/1976). Perhaps the Brazilian law should consider clarifying that the CVM must be notified to offer <b>information or advice on arbitration "involving matters within its sphere of authority" should the CVM find it advisable, and not only on court disputes.</b> This amendment is necessary to clarify the existing legal rule (article 31 of Law No. 6,385/1976).

## Notes

<sup>1</sup> Professor, INSPER and IBMEC. Partner, Monteiro de Castro, Setoguti Advogados. Coordinator of the Arbitration and Corporate Law Study Group of CBAr (Brazilian Arbitration Committee). Vice-President of IDSA (Institute of Applied Corporate Law). Coordinator of the Corporate Litigation Commission of IBRADEMP (Brazilian Institute of Business Law). Contact: [guilherme.setoguti@mcssa.com.br](mailto:guilherme.setoguti@mcssa.com.br).

<sup>2</sup> I thank Daniel Blume, Gustavo Gonzalez and Caio Figueiredo C. de Oliveira for the helpful comments on this Chapter. The opinions expressed herein are those of the author. They do not purport to reflect the opinions or views of the OECD or its members.

<sup>3</sup> References to data in this chapter were last updated on 14 July, 2020

<sup>4</sup> See Item 5, “a” and “b” of the Explanatory Memorandum of Law 6,404/1976.

<sup>5</sup> CALIXTO SALOMÃO FILHO, “Organização interna: estrutura orgânica tríplice”. In: *O novo direito societário*, 3<sup>a</sup> ed. São Paulo: Malheiros, 2006, p. 84 and “Deveres fiduciários do controlador”. In: *O novo direito societário*, 3<sup>a</sup> ed. São Paulo: Malheiros, 2006, p. 169; GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 71; JORGE LOBO, “Reforma da Lei das S.A.”. In: *A reforma da Lei das S.A.* (coord. Jorge Lobo). São Paulo: Atlas, 1998, p. 28; and EDUARDO SECCHI MUNHOZ, *Aquisição de controle na sociedade anônima*, São Paulo: Saraiva, 2013, p. 88, footnote 59, and p. 303.

<sup>6</sup> CÂNDIDO RANGEL DINAMARCO, “Sociedades anônimas e legitimidade dos minoritários – questões processuais”. In: *Processo civil empresarial*. São Paulo: Malheiros. 2010, p. 643.

<sup>7</sup> DARIO LATELLA, “Shareholder derivative suits: a comparative analysis and the implications of the European Shareholders’ Rights Directive”. *European Company and Financial Law Review*, v. 6, n. 2, 2009, p. 313; GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 72; and GABRIEL SAAD KIK BUSCHINELLI and RAFAEL HELOU BRESCIANI, “Aspectos processuais da ação de responsabilidade do controlador movida por acionista titular de menos de 5% do capital social (art. 246, § 1º, ‘b’, da Lei 6.404/76)”. In: *Processo Societário II* (coords. FLÁVIO LUIZ YARSHELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2015, p. 249.

<sup>8</sup> ALEXANDRE COUTO SILVA, *Responsabilidade dos administradores de S/A*. Rio de Janeiro: Elsevier, 2007, n. 4.16.1, p. 232; ROBERTA ROMANO, “The shareholder suit: litigation without foundation?”. *The Journal of Law, Economics & Organizations*, v. 7, n. 1, 1991, p. 57; and ROBERT CLARK, *Corporate law*. Boston: Little, Brown & Company, 1986, p. 639.

<sup>9</sup> JOSÉ LUIZ BULHÕES PEDREIRA, “Responsabilidade civil do diretor de S.A.”. In: *A Lei das S/A*, v. 2, 2ª ed. Rio de Janeiro: Renovar, 1996, p. 408; CÂNDIDO RANGEL DINAMARCO, “Sociedades anônimas e legitimidade dos minoritários – questões processuais”. In: *Processo Civil empresarial*. São Paulo: Malheiros, 2010, n. 389 e 400, p. 606 e 623, and “Sociedades anônimas e responsabilidade civil do administrador – legitimidade dos acionistas minoritários. In: *Processo Civil Empresarial*. São Paulo: Malheiros, 2010, n. 431, p. 667; JOSÉ ALEXANDRE TAVARES GUERREIRO, “Responsabilidade dos administradores de sociedades anônimas”. *RDM*, n. 42, abr./jun. 1981, p. 82 and “Conflito de interesse entre sociedade controladora e controlada e entre coligadas, no exercício do voto em assembleias gerais e reuniões sociais”, *RDM*, n. 51, 1963, p. 31; FRAN MARTINS “Ação individual de responsabilidade civil contra administradores de sociedades anônimas”. In: *Novos estudos de direito societário*. São Paulo: Saraiva, 1988, p. 144; LEONARDO PARENTONI, “Ônus da sucumbência nas ações de responsabilidade civil contra o administrador de sociedades empresárias”. In: *Sociedades anônimas e mercado de capitais – homenagem ao Prof. Osmar Brina Corrêa-Lima* (coords. ARNOLDO WALD and others). São Paulo: Quartier Latin, 2011, p. 367.

<sup>10</sup> WALDEMAR FERREIRA, *Tratado de direito comercial*, v. IV. São Paulo: Saraiva, 1961, n. 861, p. 461.

<sup>11</sup> See Section 2.1 of Prof. Gelter’s Chapter.

<sup>12</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, Section 11; VIVIANE MULLER PRADO and BRUNO M. SALAMA, “Legal protection of minority shareholders of listed corporations in Brazil: brief history, legal structure and empirical evidence”. *Journal of Civil Law Studies*, v. 4, 2011, p. 184; and PAULO CEZAR ARAGÃO, “Aspectos processuais da legislação societária”. *Revista dos Tribunais*, v. 641, mar. 1989, p. 71.

<sup>13</sup> JOSÉ MARCELO MARTINS PROENÇA and ALBERTO BARBOSA JR., “Notas sobre a revisão judicial dos atos de gestão em sociedades anônimas: os tribunais judiciais podem aprender com a CVM?”. In: *Processo societário II* (coords. FLÁVIO LUIZ YARSHELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2015 p. 373.

<sup>14</sup> ANA CAROLINA RODRIGUES, *A responsabilidade civil dos administradores de companhias abertas não financeiras por danos causados à sociedade e aos acionistas e o desenvolvimento do mercado de valores mobiliários brasileiro*. São Paulo: FGV, 2011, p. 8 and 105.

<sup>15</sup> VIVIANE MULLER PRADO and VINÍCIUS CORREA BURANELLI, *Relatório da pesquisa de jurisprudência sobre direito societário e mercado de capitais no Tribunal de Justiça de São Paulo*. Caderno Direito GV, nº 9, jan. 2006, p. 4 and 36.

<sup>16</sup> “Não custa nada mentir: desafios para o ressarcimento de investidores”, disponível em [https://www.academia.edu/28762978/N%C3%83O\\_CUSTA\\_NADA\\_MENTIR\\_desafios\\_para\\_o\\_ressarcimento\\_de\\_investidores\\_dados\\_e\\_reflexões\\_sobre\\_o\\_não\\_ressarcimento\\_de\\_investidores](https://www.academia.edu/28762978/N%C3%83O_CUSTA_NADA_MENTIR_desafios_para_o_ressarcimento_de_investidores_dados_e_reflexões_sobre_o_não_ressarcimento_de_investidores), 2016, p. 4, 13-17 and 25.

<sup>17</sup> LIONEL ZACLIS, *Proteção coletiva dos investidores no mercado de capitais*. São Paulo: RT, 2007, p. 178-182.

<sup>18</sup> VIVIANE MULLER PRADO. “Os desafios para o ressarcimento de investidores”. In: *A responsabilidade civil da empresa perante os investidores* (coords. MODESTO CARVALHOSA and others). São Paulo: Quartier Latin, 2018, p. 386-387.

<sup>19</sup> See Section 2.2. of Prof. Gelter’s Chapter.

<sup>20</sup> See Section 1 of Prof. Gelter’s Chapter with an overview on this chain of incentives and requirements against abusive derivative litigation.

<sup>21</sup> ALFREDO LAMY FILHO and JOSÉ LUIZ BULHÕES PEDREIRA, *Direito das Companhias*. Rio de Janeiro: Forense, 2017, p. 891-892; and MARCELO VON ADAMEK, *Responsabilidade Civil dos Administradores de S/A e as Ações Correlatas*. São Paulo: Saraiva, 2009, p. 319.

<sup>22</sup> “Right to Call General Meetings”

Article 123. Subject to the bylaws, general meetings shall be called by the administrative council, if any, or by the directors.

Sole Paragraph. A general meeting may also be called:

(a) by the statutory audit committee, under the provisions of item V of article 163;

(b) in accordance with the law or the bylaws, whenever the officers delay the call for more than sixty days, by any shareholder;

(c) whenever the corporation officers do not, within eight days, comply with their justifiable request that a meeting be called, indicating the matters to be discussed, by shareholders representing at least five per cent of the capital;

(d) whenever the corporation officers do not, within eight days, comply with the request that a meeting be called in order to appoint a statutory audit committee, by shareholders representing at least five per cent of the voting capital, or five per cent of nonvoting shareholders”.

<sup>23</sup> See Sections 2.4.5 of Prof. Gelter’s Chapter.

<sup>24</sup> See Section 2.4.2 of Prof. Gelter’s Chapter on minimum ownership thresholds for derivative suits in other jurisdictions.

<sup>25</sup> Pursuant to LSA article 286 the suit to annul resolutions must be filed up to two years from the date of the resolution:

“Actions to Annul Resolutions

Article 286. Proceedings to annul resolutions made at a general or special meeting of shareholders which has been called or opened otherwise than in accordance with the law or bylaws, or which has been the subject of error, bad faith, fraud or misrepresentation, shall not be commenced after a period of two years has elapsed from the date of the resolution”.

<sup>26</sup> STJ, REsp 256.596, Rel. Nancy Andrighi, DJ 18/06/2001.

<sup>27</sup> STJ, REsp 1515710, Rel. Marco Aurélio Bellizze, DJ 02/06/2015.

<sup>28</sup> MARCELO VIEIRA VON ADAMEK, *Responsabilidade civil dos administradores de S/A e as ações correlatas*. São Paulo: Saraiva, 2010, n. 6.2, p. 249-257; GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 27; ANA CAROLINA RODRIGUES, “A responsabilidade civil dos administradores de companhias abertas e a proteção dos acionistas minoritários”. *Revista de Direito Público da Economia*, n. 45, jan.mar. 2014, p. 63-64; JOSÉ MARCELO MARTINS PROENÇA and ALBERTO BARBOSA JR., “Notas sobre a revisão judicial dos atos de gestão em sociedades anônimas: os tribunais judiciais podem aprender com a CVM?”. In: *Processo*

*societário II* (coords. FLÁVIO LUIZ YARSHELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2015, p. 383-385; ALFREDO LAMY FILHO, “Responsabilidade dos administradores – atas aprovadas por assembleia geral – prescrição – ação proposta contra administrador”. In: *Temas de S/A*. Rio de Janeiro: Renovar, 2007, p. 285-292.

<sup>29</sup> “In addition to standing requirements, many jurisdictions have created a pre-trial or first stage procedure to decide about the admission of a derivative suit. The basic reason for this is the fact that the decision to bring a lawsuit on the behalf of a corporation would normally rest with the board of directors or another decision-making body within the company. Derivative suits where shareholders take this power from the board must therefore undergo special scrutiny. Pre-trial procedures serve the important function in screening out non-meritorious lawsuits and plaintiffs”.

<sup>30</sup> “Overall, an effective enforcement of derivative claims seems to rest on the presence of a mechanism that gives the initiative and control over litigation to outside shareholders and their attorneys. Such a mechanism relies on at least two factors. First, it is necessary to introduce a screening mechanism (which the US, the UK, Germany, Singapore and Israel have). Ideally, such a mechanism will weed out abusive lawsuits and permit meritorious ones to go forward. Second, their cost rules need to incentivize suits or at least not set up strong hurdles against them”.

<sup>31</sup> See Section 2.4.4 and 2.4.7 of Prof. Gelter’s Chapter.

<sup>32</sup> “Controlling Shareholder Duties

Article 116. A controlling shareholder is defined as an individual or a legal entity, or a group of individuals or legal entities by a voting agreement or under common control, which:

(a) possesses rights which permanently assure it a majority of votes in resolutions of general meetings and the power to elect a majority of the corporation officers; and

(b) in practice uses its power to direct the corporate activities and to guide the operations of the departments of the corporation. Sole Paragraph. A controlling shareholder shall use its controlling power in order to

make the corporation accomplish its purpose and perform its social role, and shall have duties and responsibilities towards the other shareholders of the corporation, those who work for the corporation and the community in which it operates, the rights and interests of which the controlling shareholder must loyally respect and heed.

<sup>33</sup> “Liability

Article 117. A controlling shareholder shall be liable for any damage caused by acts performed by the abuse of its power. Paragraph 1. An abuse of power may take any of the following forms:

(a) to guide a corporation towards an objective other than in accordance with its corporate purposes clause or harmful to national interest, or to induce it to favor another Brazilian or foreign corporation to the detriment of the shareholders’ interest in the profits or assets of the corporation or of the Brazilian economy;

(b) to provide for the liquidation of a viable corporation or for the transformation, merger or division of a corporation in order to obtain, for itself or for a third party, any undue advantage to the detriment of the other shareholders, of those working for the corporation or of investors in securities issued by the corporation;

(c) to provide for a statutory amendment, an issue of securities or an adoption of policies or decisions which are not in the best interests of the corporation but are intended to cause damage to the minority shareholders, to those working for the corporation or to investors in securities issued by the corporation:

(d) to elect a corporation officer or audit committee member known to be unfit for the position or unqualified;

(e) to induce, or attempt to induce, any officer or audit committee member to take any unlawful action, or, contrary to their duties under this Law and under the bylaws, and contrary to the interest of the corporation, to ratify any such action in a general meeting;

(f) to sign contracts with the corporation directly, through a third party or through a business in which the controlling shareholder has an interest, incorporating unduly favorable or inequitable terms;

(g) to approve, or cause to be approved, irregular accounts rendered by corporation officers as a personal favor, or to fail to verify a complaint which he knows, or should know, to be well founded, or which gives grounds to a reasonable suspicion of irregularity;

(h) to subscribe shares, for the purpose of the provision of article 170, with the contribution of property unrelated to the purpose of the corporation.

Paragraph 2. Under paragraph I (e), above, an officer or audit committee member who commits an unlawful act shall be jointly and severally liable with the controlling shareholder.

Paragraph 3. A controlling shareholder who holds the position of officer or audit committee member shall also have the duties and responsibilities relating to that position.

<sup>34</sup> See Section 1 of Prof. Gelter's Chapter.

<sup>35</sup> "The statutes differ in various details. Most require the posting of a security only if the shareholder in question holds less than 5% of shares, and several provide exemptions if the market value of shares exceeds a certain threshold (USD 25 000 or USD 50 000)" (Section 4.6.3 of Prof. Gelter's Chapter).

<sup>36</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 76.

<sup>37</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 79-80.

<sup>38</sup> WILSON DE SOUZA CAMPOS BATALHA, *Direito processual societário*. Rio de Janeiro: Forense, 1985, p. 380; and ALFREDO DE ASSIS GONÇALVES NETO, *Manual das companhias ou sociedades anônimas*, 3<sup>a</sup> ed. São Paulo: RT, 2013, n. 80, p. 154.

<sup>39</sup> STJ, REsp. 798.264, Rel. Nancy Andrighi, j. 06/02/2007; and STJ, REsp 1.214.497, Rel. Raul Araújo, j. 23/09/2014.

<sup>40</sup> STJ, REsp 16.410/SP, Rel. Sálvio Figueiredo Teixeira, DJ 16/05/1994.

<sup>41</sup> "Art. 85. The award shall order the losing party to pay the fees of the prevailing party's counsel.

(...)

§ 2º Fees shall be set at between a minimum of ten and maximum of twenty percent of the amount of the award, of the economic gain obtained or, if it cannot be measured, of the value of the claim adjusted for inflation, in accordance with:

- I – the attorney’s degree of dedication;
- II – the place where the service is rendered;
- III – the nature and importance of the claim;
- IV – the work performed by the lawyer and the time taken to perform the services”.

<sup>42</sup> “§ 6º The limits and criteria set forth in §§ 2 and 3 are applicable regardless of the content of the decision, even to cases of denial of the claim or judgment without prejudice”.

<sup>43</sup> “§ 8º In actions where the economic gain is inestimable or negligible, or even when the amount of the claim is very low, the judge shall determine the amount of counsel’s fees by means of an equitable evaluation, in compliance with the provisions of the items in § 2.”

<sup>44</sup> STJ, REsp 1.731.617, Rel. Antonio Carlos Ferreira, DJ 17.04.2018.

<sup>45</sup> LUIZ HENRIQUE VOLPI CAMARGO. *Breves Comentários ao Novo Código de Processo Civil* (coords. TERESA ARRUDA ALVIM WAMBIER and others). São Paulo: RT, 2015, p. 314; and RENATO BENEDUZI, *Comentários ao Código de Processo Civil*, arts. 70-87 (coords. LUIZ GUILHERME MARINO, SÉRGIO CRUZ ARENHART and DANIEL MITIDIERO). São Paulo: RT, 2018, p. 131-132.

<sup>46</sup> STJ, AgInt in EDcl in REsp 1436069, Rel. Marco Aurélio Bellizze, j. 04.04.2017.

<sup>47</sup> LUIZ GUILHERME MARINONI, SÉRGIO CRUZ ARENHART and DANIEL MITIDIERO. *Código de Processo Civil Comentado*, 3ª ed. São Paulo: RT, 2017; and JOSÉ ROBERTO DOS SANTOS BEDAQUE, *Código de Processo Civil Interpretado* (coord. ANTONIO CARLOS MARCATO), 3ª ed. São Paulo: Atlas, 2008, p. 76.

<sup>48</sup> STJ, REsp 1746072, Rel. Nancy Andrighi, DJ 29/03/2019; STJ, AgInt in AREsp 1197199, Rel. Ricardo Villas Bôas Cueva, DJ 25/06/2018; STJ, AgInt in AREsp 1232624, Rel. Francisco Falcão, DJ 14/05/2018; and STJ, AgInt in AREsp 1187650, Rel. Ricardo Villas Bôas Cueva, DJ 30/04/2018.

<sup>49</sup> TJSP, Ap. 1001340-45.2018.8.26.0320, Rel. Berenice Marcondes Cesar, j. 21/02/2020.

<sup>50</sup> “Art. 87. When several plaintiffs and several defendants are parties to an action, the losing parties are proportionately liable for expenses and counsel fees.

§ 1º The award must expressly distribute among the co-parties the proportional liability for the payment of the amounts set forth in the head provision”.

<sup>51</sup> GUILHERME SETOGUTI J. PEREIRA, *Curso de Arbitragem* (coords. GUILHERME SETOGUTI J. PEREIRA and DANIEL DE ANDRADE LEVY). São Paulo: RT, 2018, p. 173; CARLOS ALBERTO CARMONA. “Flexibilização do procedimento arbitral”. *Revista Brasileira de Arbitragem*. São Paulo, n. 24, out./dez. 2009, p. 12; and EDUARDO DE ALBUQUERQUE PARENTE. *Processo arbitral e sistema*. São Paulo: Atlas, 2012, p. 70 e 71.

<sup>52</sup> GABRIEL SAAD KIK BUSCHINELLI and RAFAEL HELOU BRESCIANI, “Aspectos processuais da ação de responsabilidade do controlador movida por acionista titular de menos de 5% do capital social (art. 246, § 1º, ‘b’, da Lei 6.4.04/76)”. In: *Processo Societário II* (coords. FLÁVIO LUIZ YARSELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2015.

<sup>53</sup> NELSON EIZIRIK, *A Lei das S/A comentada*, v. III. São Paulo, Quartier Latin, 2011, p. 370.

<sup>54</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 129.

<sup>55</sup> OSMAR BRINA CORRÊA-LIMA, *Responsabilidade civil dos administradores de sociedade anônima*. Rio de Janeiro: Aide, 1989, p. 115.

<sup>56</sup> ANA CAROLINA RODRIGUES, “A responsabilidade civil dos administradores de companhias abertas e a proteção dos acionistas minoritários”. *Revista de Direito Público da Economia*, n. 45, jan.mar. 2014, p. 20.

<sup>57</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 134-136.

<sup>58</sup> STJ, REsp 1.220.272-RJ, Rel. Luis Felipe Salomão, 4ª T., j. 14.12.2010.

<sup>59</sup> AMANDA ROSE, “The multienforcer approach to securities fraud deterrence: a critical analysis”. *University of Pennsylvania Law Review*, v. 158, 2010, p. 2.192.

<sup>60</sup> MARCELO TRINDADE and FABIANA MARTINS DE ALMEIDA, *The securities litigation review – Chapter 3* (Editor: William Savitt). London: Law Business Research, 2015, p. 44.

<sup>61</sup> “Art. 17. In cases of malicious prosecution, the plaintiff association and the directors responsible for filing the action will be jointly condemned to pay for court costs and counsel fees, without prejudice of liability for damages.

Art. 18. In the suits that this law concerns, there won't be advanced payment of court fees, counsel fees, costs of expert examination or any other expenses, or the liability of the plaintiff association to pay counsel costs and court fees, unless there is proven bad faith”.

<sup>62</sup> FRAN MARTINS, *Comentários à Lei das S.A.* v. III, 2ª ed. Rio de Janeiro: Forense, 1985, p. 274; NELSON EIZIRIK, *A Lei das S/A comentada*, v. III. São Paulo, Quartier Latin, 2011, v. III, p. 370; MARCELO TRINDADE and FABIANA MARTINS DE ALMEIDA, *The securities litigation review – Chapter 3* (editor William Savitt). London: Law Business Research, 2015, p. 41; and STJ, REsp 16.410-SP, Rel. Sálvio de Figueiredo Teixeira, 4ª T., DJ 16.5.1994.

<sup>63</sup> And also the thresholds foreseen in other LSA articles.

<sup>64</sup> “Pursuant to Article 291 of the Brazilian Corporate Law, CVM has authority to reduce the thresholds for larger companies, based on the capital stock stated in the company's bylaws. However, to date CVM has not issued any regulation on this matter. Reducing the threshold required to file the derivative lawsuit may help the smaller, but significant, groups of investors to litigate against management. Therefore, CVM will propose a new regulation establishing different thresholds for larger companies” (Section 2.1.2).

“Pursuant to Article 291 of the Brazilian Corporate Law, CVM may enact regulation decreasing the ownership percentage required to file the lawsuit without offering the guarantee. The less favorable treatment between shareholders owning less than 5% and those representing higher stakes have a parallel with the abovementioned rule for derivative lawsuits against managers, even though the consequences are different in each case. In both cases, the rules reveal a concern in avoiding frivolous lawsuits but may create burdens for litigation due to difficulties in achieving the minimum ownership required. As with respect to derivative litigation against managers, the WG believes that reducing this threshold may facilitate investors to bring lawsuits against controlling shareholders and will, therefore, propose new regulation suggesting different thresholds for larger companies” (Section 2.1.2).



<sup>65</sup> And also for the exercise of other rights stated in LSA.

<sup>66</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais brasileiro*. São Paulo: Quartier Latin, 2018, p. 82-84.

<sup>67</sup> CÂNDIDO RANGEL DINAMARCO, “Sociedades anônimas e legitimidade dos minoritários – questões processuais”. In: *Processo civil empresarial*. São Paulo: Malheiros. 2010, p. 625, 626 e 633; and MARCELO VIEIRA VON ADAMEK, *Responsabilidade dos administradores de S/A*. São Paulo: Saraiva, 2010, p. 492.

<sup>68</sup> “One requirement for effective enforcement is, of course, that the plaintiff have knowledge of the putative violation” (THEODOR BAUMS and KENNETH SCOTT, “Taking shareholder protection seriously? Corporate governance in the United States and Germany”. *ECGI Law Working Paper*, n. 17, 2003, p. 10, p. 51).

<sup>69</sup> The discovery period in the American Law is the one during which plaintiffs with a thin basis of evidence may rely on the defendant’s obligation to disclose pertinent information.

<sup>70</sup> GUIDO FERRARINI and PAOLO GIUDICI, “Financial Scandals and the Role of Private Enforcement: The Parmalat Case”. *ECGI Working Paper Series in Law*, n. 40, 2005, p. 51 e 53.

<sup>71</sup> JOHN COFFEE JR., *Entrepreneurial litigation – its rise, fall, and future*. Cambridge: Harvard Press, p. 3 e 200; ÉRICA GORGA, “Is US law enforcement stronger than of a developing country? The case of securities fraud by Brazilian corporations and lessons for the private and public enforcement debate”. *Columbia Journal of Transnational Law*, v. 54, n. 3, 2016 p. 657; BERNARD BLACK, “The core institutions that support strong securities markets”. *The Business Lawyer*, v. 55, ago. 2000, p. 1.588 e 1.589; and ÉRICA GORGA and MICHAEL HALBERSTAM, “Litigation discovery & corporate governance: the missing story about ‘the genius of American corporate law’”. *Emory Law Journal*, v. 63, 2014, p. 1.394 e 1.395.

<sup>72</sup> GUILHERME SETOGUTI J. PEREIRA, *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, Section 19.2.

<sup>73</sup> BRUNO SALAMA and VIVIANE MULLER PRADO, “Legal protection of minority shareholders of listed corporations in Brazil: brief history, legal structure and empirical evidence”. *Journal of Civil Law Studies*, v. 4, 2011, p. 152-155.

<sup>74</sup> MODESTO CARVALHOSA and NELSON EIZIRIK, *A nova Lei das S/A*. São Paulo: Saraiva, 2002, p. 2.

<sup>75</sup> ANGELA RITA FRANCO DONAGGIO, JULYA SOTTO MAYOR WELLISCH and TATIANA FLORES SERAFIM, “Desenvolvimento do mercado de capitais brasileiro: o Novo Mercado”. In: *Mercado de capitais brasileiro II* (coord. MAURO RODRIGUES PENTEADO). São Paulo: Quartier Latin, 2015, p. 242-272.

<sup>76</sup> VIVIANE MULLER PRADO, “Não custa nada mentir: desafios para o ressarcimento de investidores”, [https://www.academia.edu/28762978/N%C3%83O\\_CUSTA\\_NADA\\_MENTIR\\_desafios\\_para\\_o\\_ressarcimento\\_de\\_investidores](https://www.academia.edu/28762978/N%C3%83O_CUSTA_NADA_MENTIR_desafios_para_o_ressarcimento_de_investidores) dados e reflexões sobre o não ressarcimento de investidores”, 2016, p. 2.

<sup>77</sup> UINIE CAMINHA, “Arbitragem como instrumento de desenvolvimento do mercado de capitais”. In: *Arbitragem institucional – 12 anos da Lei 9.307/1996* (org. HAROLDO MALHEIROS VERÇOSA). São Paulo: Malheiros. 2008, p. 94, 95 e 106-10; MARIA HELENA SANTANA, “O Novo Mercado” (2008), <http://www.bmfbovespa.com.br/pdf/Focus5.pdf>, p. 14); and HAROLDO MALHEIROS VERÇOSA, “A arbitragem e o mercado de capitais”. *RDM*, n. 146, abr./jun. 2007, p. 160.

<sup>78</sup> The data collected in September, 2018 showed that, since the beginning of its activities in 2001, the chamber had conducted a total of 116 proceedings (51 in course, 65 concluded), with 79 of the disputes related to corporate law issues, such as annulment of shareholders meeting decisions, recovery of damages caused by contractual breaches or wrongdoing by the company management. The Interim Report also explains that, among the 79 proceedings discussing corporate law issues, (i) 20 proceedings involved companies listed in special segments in which the use of arbitration is mandatory; (ii) 6 involve publicly-held companies not listed in the referred listing segments, but which also had included in their bylaws arbitration agreements; and (iii) the 53 remaining proceedings involve parties that voluntarily decided to submit the issue to arbitration at the Chamber. Eleven of the 79 proceedings (13.94%) were initiated by minority shareholders demanding redress from controlling shareholders or from the company itself, all of which remain pending. Four of the 11 were based on Article 246 of the Brazilian Corporate Law providing for minority shareholders to seek damages from controlling shareholders without submitting the matter to a general shareholder meeting.

<sup>79</sup> “Almost 70% of the cases administered by the institution from 2010 to 2019 were related to shareholders’ disputes. In 2019, according to the data provided by e-mail, the arbitral institution received 27 new requests for arbitration, 59% of them dealt with internal company disputes, including 2 class arbitrations”.

<sup>80</sup> SELMA LEMES, ADRIANA BRAGHETTA, DANIELA GABBAY, ELEONORA PITOMBO and K. “Arbitragem e Poder Judiciário: uma radiografia dos casos que chegam ao Judiciário brasileiro”. *Cadernos Direito GV*, v. 6, n. 6, nov. 2009; CBAR-COMITÊ BRASILEIRO DE ARBITRAGEM. *Separata – Arbitragem no Brasil – Pesquisa CBar-Ipsos*. São Paulo: IOB, 2012; and SELMA LEMES, *Análise da Pesquisa Arbitragem em Números de 2010 a 2013*,

<http://selmalemes.adv.br/artigos/An%C3%A1lise%20da%20Pesquisa%20Arbitragem%20em%20N%C3%BAmeros%20-2010-2013.pdf>

<sup>81</sup> ÉRICA GORGA, “A cultura brasileira como fator determinante na governança corporativa e no desenvolvimento do mercado de capitais”. *Revista de Administração*, v. 39, out./dez. 2004, p. 310.

<sup>82</sup> “O Novo Mercado. The World Bank Group”, 2008, p. 14, <http://www.bmfbovespa.com.br/pdf/Focus5.pdf>.

<sup>83</sup> CALIXTO SALOMÃO FILHO, “Direito societário e Novo Mercado”. In: *O novo direito societário*, 3ª ed. São Paulo: Malheiros, 2006, p. 59.

<sup>84</sup> Article 1.4 (<http://www.ibgc.org.br/userfiles/2014/files/CMPGPT.pdf>).

<sup>85</sup> Article III.6 (<http://www.cvm.gov.br/export/sites/cvm/deciso/es/anexos/0001/3935.pdf>).

<sup>86</sup> “Characteristic of so many of the suits under Rule 10b-5 for false corporate announcements by a publicly traded company is that most purchasers or sellers have relatively small amounts at stake. When there are numerous investors who have suffered a common misrepresentation, the class action device is often the only economically viable means of achieving the compensatory and deterrent goals underlying private action” (JAMES D. COX, ROBERT HILLMAN and DONALD LANGEVOORT, *Securities regulation*, 7ª ed. New York: Kluwer, 2013, p. 789). See also IAN HUNTER and LOUIS FLANNERY, “Class action and arbitration procedures – United Kingdom”. In: *Class arbitration in the European Union* (Editor: Phillippe Billiet). Antwerpen: Maklu, 2013, p. 185.

<sup>87</sup> WILLIAM SAVITT and NOAH YAVITZ, *The securities litigation review – Chapter 14* (ed. William Savitt). London: Law Business Research, 2015, p. 182; and GUILHERME SETOGUTI J. PEREIRA. *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, p. 172.

<sup>88</sup> ADA PELLEGRINI GRINOVER, *Código Brasileiro de Defesa do Consumidor comentado pelos autores do Anteprojeto*, 6ª ed. Rio de Janeiro: Forense, 1999, p. 767; CAMILO ZUFELATO, “Tutela jurisdicional coletiva dos investidores no mercado de capitais e dos sócios minoritários e a judicialização da negativa de fusão entre Pão de Açúcar e Carrefour”. *Revista de Processo*, v. 233, jul. 2014, p. 185; ANTONIO GIDI, *Coisa julgada e litispendência em ações coletivas*. São Paulo: RT, 1995, p. 138, footnote 333; and MÁRCIA TANJI, *Mercado de capitais brasileiro e tutela coletiva dos interesses*. São Paulo: USP, 2009, p. 158.

<sup>89</sup> LIONEL ZACLIS, *Proteção coletiva dos investidores no mercado de capitais*. São Paulo: RT, 2007, p. 178-183.

<sup>90</sup> JOHN COFFEE JR., *Entrepreneurial litigation – its rise, fall, and future*. Cambridge: Harvard Press, 2015, p. 167.

<sup>91</sup> ALEXANDRE PINHEIRO DOS SANTOS, FÁBIO MEDINA OSÓRIO and JULYA SOTTO MAYOR WELLISCH, *Mercado de capitais – regime sancionador*. São Paulo: Saraiva, 2012, p. 160; WILGES BRUSCATO, “A proteção judicial aos investidores no mercado de valores mobiliários”. *RDM*, n. 138, jun. 2005, p. 44; DANILO AUGUSTO BARBOZA DE AGUIAR, “Proteção dos acionistas minoritários das sociedades anônimas abertas como forma de promover o desenvolvimento do mercado de capitais nacional”. *Revista de Direito Bancário, do Mercado de Capitais e da Arbitragem*, n. 22, out./dez. 2003, p. 115; CAMILO ZUFELATO, “Tutela jurisdicional coletiva dos investidores no mercado de capitais e dos sócios minoritários e a judicialização negativa de fusão entre Pão de Açúcar e Carrefour”. *Revista de Processo*, v. 233, jul. 2014, p. 192; and MAYARA GASPAROTO TONIN and MAYARA ROTH ISFER, “Apontamentos sobre a efetividade do sistema de aplicação da lei (*enforcement*) no mercado de valores mobiliários brasileiro”. *Revista de Direito Empresarial*, v. 9, mai./jun. 2015, p. 274.

<sup>92</sup> [https://www.investidorpetrobras.com.br/ptb/16375/Formulario-de-Referencia-2018-2019\\_V30.pdf](https://www.investidorpetrobras.com.br/ptb/16375/Formulario-de-Referencia-2018-2019_V30.pdf)

<sup>93</sup> <https://oglobo.globo.com/economia/investidores-iniciam-acao-arbitral-contra-vale-por-cao-do-acidente-em-brumadinho-23814997>

<sup>94</sup> <http://www.vale.com/PT/investors/information-market/annual-reports/reference-form/Documents/docs-pt/Vale%20Formul%C3%A1rio%20de%20Refer%C3%Aancia%20-%20Vers%C3%A3o%2022.pdf>

<sup>95</sup> <https://valor.globo.com/financas/noticia/2020/03/18/investidores-iniciam-arbitragem-contra-o-irb.ghtml>

<sup>96</sup> This Report has analyzed the arbitration rules of CAM-CCBC, Market Arbitration Chamber/B3, CIESP-FIESP, CAMARB, FGV, CCI and AMCHAM.

<sup>97</sup> “9.7. The associative entity, including the one that represents its members by means of authorization in the form of article 5, XXI, of the Federal Constitution, is considered a unique Party.

9.8. In the case of representation provided in Article 5, XXI, of the Federal Constitution, the provisions on the addition of third parties apply to the addition of other associates to be represented by the associative entity, whether if the association to the entity is supervenient to the arbitration or not. It will be up to the entity, if applicable, to initiate a different procedure in favor of the other associates if their entry into the ongoing procedure is not admitted. In this case, it will be possible to reunion of arbitrations, if the other applicable requirements are met.”

<sup>9898</sup> For other countries’ experience, see EDWARD DOLIDO, “Confidentiality during and after arbitration”. In: *American Arbitration Association handbook on commercial arbitration*, 2ª ed. New York: Juris Net, 2010, p. 399; and GABRIELE CRESPI REGHIZZI and MATTEO DRAGONI, “Class actions and arbitration in the

European Union – Italy”. In: *Class arbitration in the European Union* (editor. Philippe Billiet). Antwerpen: Maklu, 2013, p. 133).

<sup>99</sup> FRANCISCO JOSÉ CAHALI, *Curso de arbitragem*, 3ª ed. São Paulo: RT, p. 240.

<sup>100</sup> MARGARET L. MOSES, *The principles and practice of international commercial arbitration*. 2ª ed. Cambridge: Cambridge University Press, p. 4; GARY B. BORN, *International arbitration: law and practice*. Netherlands: Kluwer, 2012, p. 15; ARNOLDO WALD, “A reforma da Lei das Sociedades Anônimas: os direitos dos minoritários na Nova Lei das S/A”. In: *Reforma da Lei das Sociedades Anônimas* (coord. JORGE LOBO). Rio de Janeiro: Forense, 2002, p. 238); and JOHN H. HENN, “Where should you litigate your business dispute? In an arbitration or through the courts?”. In: *American Arbitration Association handbook on commercial arbitration*, 2ª ed. New York: Juris Net. 2010, pp. 325/326.

<sup>101</sup> *Separata – Arbitragem no Brasil – Pesquisa CBAr-Ipsos*, São Paulo, IOB, 2012, p. 12.

<sup>102</sup> CHRISTINA BEYRODT CARDOSO, LEONARDO DE C. COELHO and THIAGO RODOVALHO, “Poderes, deveres e jurisdição de um tribunal arbitral”. In: *Arbitragem comercial. Princípios, instituições e procedimentos. A prática no CAM-CCBC* (coords. MARISTELA BASSO and FABRÍCIO POLIDO). São Paulo: Marcial Pons. 2013, p. 233).

103

<http://www.bmfbovespa.com.br/lumis/portal/file/fileDownload.jsp?fileId=8A828D294E6F7F51014E734202294677>.

104

<http://www.bmfbovespa.com.br/lumis/portal/file/fileDownload.jsp?fileId=8A828D294E6F7F51014E7342026E46C8>.

<sup>105</sup> GUILHERME SETOGUTI J. PEREIRA. “Termos que repensar a confidencialidade das arbitragens societárias”. In: *Processo societário III* (coords. FLÁVIO LUIZ YARSELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2018, p. 226-228.

<sup>106</sup> RÔMULO GREFF MARIANI, *Arbitragens coletivas no Brasil*. São Paulo: Atlas, 2015, p. 192 and 199.

<sup>107</sup> The advantages of adopting an opt out system or not is also something that needs to be better addressed.

<sup>108</sup> GUILHERME SETOGUTI J. PEREIRA. “Termos que repensar a confidencialidade das arbitragens societárias”. In: *Processo societário III* (coords. FLÁVIO LUIZ YARSELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2018, p. 227.

<sup>109</sup> ÉRICA GORGA, “Is US law enforcement stronger than of a developing country? The case of securities fraud by Brazilian corporations and lessons for the private and public enforcement debate”. *Columbia Journal of Transnational Law*, v. 54, n. 3, 2016, p. 668.

<sup>110</sup> MARCELO TRINDADE, “O papel da CVM e o mercado de capitais no Brasil”. In: *Fusões e aquisições: aspectos jurídicos e econômicos* (org. Jairo Saddi). São Paulo: IOB, 2002, p. 309); ANDRÉ GRÜNSPUN PITTA, *O regime de informação das companhias abertas*. São Paulo: Quartier Latin, 2013, p. 67; and ANDRÉ ANTUNES SOARES DE CAMARGO, *Revista de Direito Bancário e do Mercado de Capitais*, n. 38, out./dez. 2007, p. 106-112.

<sup>111</sup> MARIANA PARGENDLER, VIVIANE MULLER PRADO and ALBERTO BARBOSA JR., “Cláusulas arbitrais no mercado de capitais brasileiro: alguns dados empíricos”. *Revista de Arbitragem e Mediação*, n. 40, 2014, p. 107; ANA TEREZA BASILIO and THIAGO LINS. “A relativização da confidencialidade na arbitragem: companhias abertas”. *Revista de Arbitragem e Mediação*, v. 49, abr./jun., 2016, p. 168; and EDUARDO SECCHI MUNHOZ, “A importância do sistema de solução de conflitos para o direito societário: limites do instituto da arbitragem”. In: *Processo societário* (coords. FLÁVIO LUIZ YARSHELL e GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin: 2012, p. 91 e 92).

<sup>112</sup> ALEX HATANAKA, “Limites da confidencialidade na arbitragem envolvendo sociedades por ações de capital aberto”. *Revista de Direito das Sociedades e dos Valores Mobiliários*, v. 3, maio 2016, p. 121 e 122.

<sup>113</sup> RÔMULO GREFF MARIANI, *Arbitragens coletivas no Brasil*. São Paulo: Atlas, 2015, p. 198; and ANA LUIZA NERY, *Arbitragem coletiva*. São Paulo: RT, 2016, p. 279, 292 and 306.

<sup>114</sup> This is the reason why Profs. Monteiro and Beneduzi’s Chapter states that is “practically impossible to address a collective or mass claim through arbitration in England and Wales without significant legislative change”, considering that “English law implies the confidentiality of the arbitral proceedings” (Section 9).

<sup>115</sup> “7.10 From time to time the Arbitration Chamber shall publish a Summary of Arbitral Awards. Such summaries shall be grouped by the topics involved and may be taken into consideration by arbitrators as mere reference material to orient their decisions. Published awards shall omit any elements that enable the proceedings to be identified.”

<sup>116</sup> GUILHERME SETOGUTI J. PEREIRA. “Termos que repensar a confidencialidade das arbitragens societárias”. In: *Processo societário III* (coords. FLÁVIO LUIZ YARSHELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2018, p. 237-239.

<sup>117</sup> JAMS Rules also provide for the notice of class determination (s. 4).

<sup>118</sup> AAA Supplementary Rules for Class Arbitrations. Rule 6. Notice of Class Determination. (...). (b) The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class judgment on class members.

<sup>119</sup> JAMS Class Action Procedures. Rule 4. Notice of Class Determination. (...). The Notice of Class Determination must concisely and clearly state in plain, easily understood language (...) (6) the binding effect of a class award on class members.

<sup>120</sup> See Section 3 of Profs. Monteiro and Beneduzi’s Chapter.

<sup>121</sup> “In this case, the rules of arbitration of the arbitral institution should define specific opportunities and the corresponding time periods for that. According to the AAA Supplementary Rules for Class Arbitrations and the JAMS Class Action Procedures, shareholders have two opportunities to exercise their right to opt-out: (i) after being notified of the commencement of the class arbitration (Rules 6(b)(5); and Rule 4(5)) and (ii) after being notified of the purposed terms of a settlement (Rule 8(c); and Rule 6(c))” (Section 12.5 of Profs. Monteiro and Beneduzi’s Chapter).

<sup>122</sup> In Italy the request for arbitration involving a corporate dispute must be published in the business register, in order to give publicity and facilitate the intervention of third parties (art. 35, par. 1 *Decreto Legislativo* 5 of 2003).

<sup>123</sup> GUILHERME SETOGUTI J. PEREIRA. *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, p. 167.

<sup>124</sup> This explains why Profs. Monteiro and Beneduzi wrote that “The intervention of third parties and other shareholders may be indirectly facilitated by the rule under which the request of arbitration needs to be published in the business register” pursuant to the Italian law (Section 5).

<sup>125</sup> “If the case regards the annulment of shareholders’ resolutions or if the arbitral decision is capable of binding people who were not formal parties to the arbitration, s. 6(3) imposes on the claimant the duty to list all potentially affected people, who will be notified of the case. They have the right to intervene in the ongoing arbitration as a co-claimant or as a co-respondent (s. 7(2))” (Section 3.6 of Profs. Monteiro and Beneduzi’s Chapter).

<sup>126</sup> ELEONORA COELHO, “Necessidade de criação de regulamentos adaptados para arbitragens coletivas no mercado de capitais”. In: *Processo societário III* (coords. FLÁVIO LUIZ YARSHELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2018, p. 133.

<sup>127</sup> “JOINDER OF PARTIES AND CONSOLIDATION OF PROCEEDINGS

6.1 Joinder of parties. Before any arbitrators have been appointed, the parties may request the inclusion of one or more additional parties in the arbitration proceedings by filing a Motion for Joinder of Parties (“Motion for Joinder”). Third parties with a legitimate claim to join or intervene in the proceedings may request permission to do so by filing a Motion for Joinder.

6.1.1. Motions for Joinder shall be submitted to the Arbitration Tribunal’s Secretariat. They shall contain a justification for requiring the inclusion of additional parties and be accompanied by copies of the Request for Arbitration and the Answer or Answers thereto.

6.1.2 Answers to Motions for Joinder must be filed within fifteen (15) days and shall comply with the provisions of 2.1.3 above.

6.1.3 The parties shall be directed to respond to the Answers to Motions for Joinder within ten (10) days.

6.1.4 The President of the Arbitration Chamber shall decide whether to accept a Motion for Joinder. If he accepts it, the joined party shall enter the arbitration proceedings at that point, signing an undertaking to comply with these Rules and to be bound by the arbitral award. Should any party object and if the President of the Arbitration Chamber overrides such objection, enforcing the Motion for Joinder, the Arbitration Tribunal shall review the matter and issue a final decision regarding the joinder.”

<sup>128</sup> For example, the CPC allows the intervention of third parties that are not bound by the arbitration agreement, which in principle is not admissible in arbitration. Third party intervention in court proceedings are usually public, whereas arbitral proceedings are usually confidential, and these differences have important effects on how a third party can join or be summoned to participate in the proceeding. Another distinction: in court proceedings the judge is designated according to the court rules and if a third party joins the proceeding the fact does not impact on the designation of the judge. In arbitration, however, if a third party joins the proceeding it may impact the arbitral tribunal constitution.

<sup>129</sup> RÔMULO GREFF MARIANI, *Arbitragens coletivas no Brasil*. São Paulo: Atlas, 2015, p. 199; and ANA LUIZA NERY, *Arbitragem coletiva*. São Paulo: RT, 2016, p. 255 and 305.

<sup>130</sup> YVES DERAIS and AURORE DESCOMBES, “Class actions and arbitration in the European Union – France”. In: *Class arbitration in the European Union* (editor. Philippe Billiet). Antwerpen: Maklu, 2013, p. 40.

- <sup>131</sup> CAROLINE COSTA, SÍLVIA CRISTINA SALATINO and THIAGO ALVES FERREIRA DOS SANTOS, “A instalação e organização de um tribunal arbitral”. In: *Arbitragem comercial. Princípios, instituições e procedimentos. A prática no CAM-CCBC* (coords. MARISTELA BASSO e FABRÍCIO POLIDO). São Paulo: Marcial Pons. 2013, p. 168).
- <sup>132</sup> LARRY ENGEL, “Commercial arbitration: winning over the skeptics”. In: *American Arbitration association handbook on commercial arbitration*, 2ª ed. New York: Juris Net. 2010, p. 18.
- <sup>133</sup> GUILHERME SETOGUTI J. PEREIRA. *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, p. 170.
- <sup>134</sup> ELEONORA COELHO, “Necessidade de criação de regulamentos adaptados para arbitragens coletivas no mercado de capitais”. In: *Processo societário III* (coords. FLÁVIO LUIZ YARSELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo: Quartier Latin, 2018, p. 138.
- <sup>135</sup> <https://a.storyblok.com/f/46533/x/644d9d61e0/discussao-anteprojeto-diploma-legislativo-regras-arb-materia-societaria.pdf>
- <sup>136</sup> <https://a.storyblok.com/f/46533/x/96f24127f1/discussao-anteprojeto-regulamento-arb-societaria-p-centros-arb.pdf>
- <sup>137</sup> RODRIGO TELLECHEA, *Arbitragem nas sociedades anônimas – direitos individuais e princípio majoritário*. São Paulo: Quartier Latin, 2016, p. 346.
- <sup>138</sup> GU WEIXIA, “Securities arbitration in China: a better alternative to retail shareholder protection”. *Northwestern Journal of International Law & Business*, v. 33, 2012-2013, p. 308; and BRUNO SALAMA, “Análise econômica da arbitragem”. In: *Direito e economia no Brasil* (coord. LUCIANO BENETTI TIMM). São Paulo: Atlas, 2012, p. 383-384).
- <sup>139</sup> RODRIGO TELLECHEA, *Arbitragem nas sociedades anônimas – direitos individuais e princípio majoritário*. São Paulo: Quartier Latin, 2016, p. 347.
- <sup>140</sup> GUILHERME CARDOSO SANCHEZ and GUILHERME SETOGUTI J. PEREIRA, “Sócios minoritários e a arbitragem societária”. *Valor Econômico*, 26.04.12.
- <sup>141</sup> ADA PELLEGRINI GRINOVER, “A tutela jurisdicional dos interesses difusos no direito comparado”. In: *A tutela dos interesses difusos* (coord. ADA PELLEGRINI GRINOVER). São Paulo: Max Limonad, 1984, p. 78.
- <sup>142</sup> ANTONIO GIDI, “A representação adequada nas ações coletivas brasileiras: uma proposta”. *Revista de Processo*, n. 108, out./dez. 2002, p. 66; ADA PELLEGRINI GRINOVER, “A tutela coletiva dos investidores no mercado de valores mobiliários: questões processuais”. In: *Processo societário* (coords. FLÁVIO LUIZ YARSELL and GUILHERME SETOGUTI J. PEREIRA). São Paulo, Quartier Latin, 2012, p. 48 and “Novas questões sobre a legitimação e a coisa julgada nas ações coletivas”. In: *O processo – estudos e pareceres*, 2ª ed. São Paulo: DPJ, 2009, p. 267; RODRIGO MENDES DE ARAÚJO, *A representação adequada nas ações coletivas*. Salvador: Jus Podivm, 2013, p. 221; and FREDIE DIDIER JR. and HERMES ZANETTI JR., *Curso de direito processual civil*, v. 4, 10ª ed. Salvador: Jus Podivm, 2016, p. 186-190.
- <sup>143</sup> VIVIANE SIQUEIRA RODRIGUES, *O processo coletivo para a defesa dos direitos individuais homogêneos*. São Paulo: USP, 2012 p. 87.
- <sup>144</sup> FREDIE DIDIER JR. and HERMES ZANETTI JR., *Curso de direito processual civil*, v. 4, 10ª ed. Salvador: Jus Podivm, 2016, p. 188.

<sup>145</sup> “Rule 3. Prerequisites to a Class Certification.

(a) The Arbitrator shall determine whether a class should be certified.

In making that determination, the Arbitrator shall consider the criteria enumerated in this Rule 3 and any law that the Arbitrator determines applicable to the arbitration. The Arbitrator shall also determine whether one or more members of a class may act in the arbitration as representative parties on behalf of all members of the class described. The Arbitrator shall permit a class member to serve as a representative only if the conditions set forth in the Federal Rules of Civil Procedure, Rule 23(a), are met.

(b) Class Actions Maintainable. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, in addition to the criteria set forth in the Federal Rules of Civil Procedure, Rule 23(b).

(c) The Arbitrator shall set forth a determination with respect to the matter of Class Certification in a partial final award subject to immediate court review.”

<sup>146</sup> “Rule 23. Class Actions

1.1. Primary tabs

(a) Prerequisites. One or more members of a class may sue or be sued as representative parties on behalf of all members only if:

(1) the class is so numerous that joinder of all members is impracticable;

(2) there are questions of law or fact common to the class;

(3) the claims or defenses of the representative parties are typical of the claims or defenses of the class; and

(4) the representative parties will fairly and adequately protect the interests of the class.”

<sup>147</sup> “(g) Class Counsel.

(1) *Appointing Class Counsel*. Unless a statute provides otherwise, a court that certifies a class must appoint class counsel. In appointing class counsel, the court:

(A) must consider:

(i) the work counsel has done in identifying or investigating potential claims in the action;

(ii) counsel's experience in handling class actions, other complex litigation, and the types of claims asserted in the action;

(iii) counsel's knowledge of the applicable law; and

(iv) the resources that counsel will commit to representing the class;

(B) may consider any other matter pertinent to counsel's ability to fairly and adequately represent the interests of the class;

(C) may order potential class counsel to provide information on any subject pertinent to the appointment and to propose terms for attorney's fees and nontaxable costs;

(D) may include in the appointing order provisions about the award of attorney's fees or nontaxable costs under Rule 23(h); and

(E) may make further orders in connection with the appointment.

(2) *Standard for Appointing Class Counsel*. When one applicant seeks appointment as class counsel, the court may appoint that applicant only if the applicant is adequate under Rule 23(g)(1) and (4). If more than one adequate applicant seeks appointment, the court must appoint the applicant best able to represent the interests of the class.



(3) *Interim Counsel*. The court may designate interim counsel to act on behalf of a putative class before determining whether to certify the action as a class action.

(4) *Duty of Class Counsel*. Class counsel must fairly and adequately represent the interests of the class.”

<sup>148</sup> “(iii) Rebuttable presumption

(I) In general. Subject to subclause (II), for purposes of clause (i), the court shall adopt a presumption that the most adequate plaintiff in any private action arising under this chapter is the person or group of persons that:

(aa) has either filed the complaint or made a motion in response to a notice under subparagraph (A)(i);  
 (bb) in the determination of the court, has the largest financial interest in the relief sought by the class; and  
 (cc) otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure.

(II) Rebuttal evidence. The presumption described in subclause (I) may be rebutted only upon proof by a member of the purported plaintiff class that the presumptively most adequate plaintiff—

(aa) will not fairly and adequately protect the interests of the class; or  
 (bb) is subject to unique defenses that render such plaintiff incapable of adequately representing the class.”

<sup>149</sup> “(v) Selection of lead counsel: The most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class.”

<sup>150</sup> SAMUEL ISSACHAROFF and GEOFFREY MILLER, “Will aggregate litigation come to Europe?”, *Vanderbilt Law Review*, v. 69, 2009, p. 196 and 197; ROBIN HUI HUANG, “Private enforcement of securities law in China: a ten-year retrospective and empirical assessment”. *The American Journal of Comparative Law*, v. 61, 2013, p. 787; ANTONIO GIDI, *A class action como instrumento de tutela coletiva dos direitos*. São Paulo: RT, 2007, p. 248; and WILLIAM BRATTON and MICHAEL WACHTER, “The political economy of fraud on the Market”. *University of Pennsylvania Law Review*, v. 169, 2011 p. 143.

<sup>151</sup> CENTO TELJANOVSKI, “Third-party funding in Europe”. *Journal of Law, Economics & Policy*, v. 3, 2012, p. 405-449; VICTORIA SHANNON, “Harmonizing third-party litigation funding regulation”. *Cardozo Law Review*, v. 36, 2015, p. 861-912; MAYA STEINITZ, “Whose claim is this anyway – third-party litigation funding”. *Minnesota Law Review*, v. 95, 2011, p. 1.268-1.338; RONEN AVRAHAM, “Third-party litigation funding – a signaling model”. *DePaul Law Review*, v. 63, 2014, p. 233-264; and RAFAEL FRANCISCO ALVES and LÍGIA VERONESE, “Arbitragem e empresas em crise: o acesso à Justiça e o cumprimento da convenção de arbitragem em vista da incapacidade financeira de uma das partes”. *Revista do Advogado*, n. 131, out. 2016, p. 178.

<sup>152</sup> See Section 4 of Profs. Monteiro and Beneduzi’s Chapter.

<sup>153</sup> NAPOLEÃO CASADO FILHO, *Arbitragem comercial internacional e acesso à justiça: o novo paradigma do third party funding* (tese de doutorado). São Paulo: PUCSP, 2014, p. 133-134.

<sup>154</sup> CAM-CCBC Administrative Resolution 18/2016 (<http://www.ccbc.org.br/Materia/2890/resolucao-administrativa-182016>).

<sup>155</sup> GUILHERME SETOGUTI J. PEREIRA. *Enforcement e tutela indenizatória no direito societário e no mercado de capitais*. São Paulo: Quartier Latin, 2018, p. 138.

<sup>156</sup> *O moderno processo civil* (transl. TERESA ARRUDA ALVIM WAMBIER), 2ª ed. São Paulo: RT, 2012, p. 310.

<sup>157</sup> DANIELA PERETTI D’ÁVILA, *A atuação da Comissão de Valores Mobiliários como amicus curiae nos processos judiciais que envolvem o mercado de capitais*. São Paulo: Almedina, 2015, p. 55-60.

<sup>158</sup> ADEMAR VIDAL NETO, *Comentários à Lei do Mercado de Capitais – Lei nº 6.385/76* (coords. LAURA PATELLA and GABRIELA CODORNIZ). São Paulo: Quartier Latin, 2015, p. 665.

<sup>159</sup> EDUARDO TALAMINI, *Breves comentários ao novo Código de Processo Civil* (coords. TERESA ARRUDA ALVIM WAMBIER, FREDIE DIDIER JR., EDUARDO TALAMINI and BRUNO DANTAS). São Paulo: RT, 2015, p. 439.

<sup>160</sup> CÉSAR AUGUSTO DI NATALE NOBRE, “*Amicus curiae*: uma abordagem processual da figura no âmbito da CVM e do CADE”. *Revista Dialética de Direito Processual*, n. 132, mar. 2014, p. 37; and OSVALDO HAMILTON TAVARES, “A CVM como ‘amicus curiae’”. *Revista dos Tribunais*, v. 690, abr. 1993, p. 287.

<sup>161</sup> DANIELA PERETTI D’ÁVILA, *A atuação da Comissão de Valores Mobiliários como amicus curiae nos processos judiciais que envolvem o mercado de capitais*. São Paulo: Almedina, 2015, p. 79-88.

<sup>162</sup> RENATO BENEDUZI, *Comentários ao Código de Processo Civil*, v. II (coords. LUIZ GUILHERME MARINONI, SÉRGIO CRUZ ARENHART and DANIEL MITIDIERO). São Paulo: RT, 2016, p. 270.

<sup>163</sup> CÁSSIO SCARPINELLA BUENO, *Novo Código de Processo Civil anotado*. São Paulo: Saraiva, 2015, p. 136.

<sup>164</sup> *Entrepreneurial litigation – its rise, fall, and future*. Cambridge: Harvard Press. 2015, p. 224 e 234.

<sup>165</sup> CÉSAR AUGUSTO DI NATALE NOBRE, “*Amicus curiae*: uma abordagem processual da figura no âmbito da CVM e do CADE”. *Revista Dialética de Direito Processual*, n. 132, mar. 2014, p. 39-42.

<sup>166</sup> CAMILO ZUFELATO, “Tutela jurisdicional coletiva dos investidores no mercado de capitais e dos sócios minoritários e a judicialização da negativa de fusão entre Pão de Açúcar e Carrefour”. *Revista de Processo*, v. 233, jul. 2014, p. 202; and EDUARDO CÂNDIA, “Tutela jurisdicional coletiva dos investidores no mercado de valores mobiliários: quem são os colegitimados ativos para a ação civil pública?”. *Revista de Direito Bancário e do Mercado de Capitais*. v. 52, abr./jun. 2011, p. 118.

<sup>167</sup> “the collective nature of the dispute may justify the supervision of the proceedings by the CVM under art. 31 of *Lei 6.385/76*. In practical terms, the rules of arbitration of the arbitral institution should empower the arbitral tribunal to notify the securities and exchange authority of the commencement of the arbitral proceedings” (Section 12.5 of Chapter 3).



The G20/OECD Principles of Corporate Governance state that “experience has shown that an important determinant of the degree to which shareholder rights are protected is whether effective methods exist to obtain redress for grievances at a reasonable cost and without excessive delay”. The G20/OECD Principles also highlight that “there is some risk that a legal system which enables any investor to challenge corporate activity in the courts can become prone to excessive litigation”. Consequently, legislators and regulators must strike a balance between adequate incentives for investors to find redress for infringement of their ownership rights and avoiding frivolous litigation that may drain valuable resources from companies.

Building on a comparative review of frameworks from nine other countries – France, Germany, Israel, Italy, Portugal, Singapore, Spain, the US and the UK – this OECD report, *Private Enforcement of Shareholder Rights*, recommends a range of actions to address weaknesses in the frameworks for derivative suits and arbitration in Brazil. Policy alternatives offered for Brazil seek to address procedural barriers that minority shareholders must surpass before filing derivative claims. Likewise, the cost allocation between the winning and losing parties serves as another important disincentive for effective private enforcement through derivative lawsuits. Finally, an arbitration framework designed mainly for commercial disputes with two parties might not work adequately for collective or multi-party corporate arbitrations, where, for example, confidentiality creates a number of challenges.

[www.oecd.org/corporate](http://www.oecd.org/corporate)

