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Private Civil Actions and Alternative Dispute Resolution

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As a lawyer, I have always described my career as a permanent effort to know a little bit more of a little bit less of the law or, more specifically, of Brazilian law. This has been a very tiresome, while personally and professionally rewarding effort, that, at the same time, is exactly the opposite of the professional and personal challenge of Brazilian lower and upper court judges, who are daily required to draft opinions on the most diverse subjects one can think of.

Indeed, at least in Brazil, which as you know is a civil Law country, the same federal lower court could be required to adjudicate issues related to tax law, criminal law, corporate and securities regulation, social security law, administrative law, environmental law and other matters.

This all-encompassing knowledge is obviously beyond the ability of even an above average human being and jurist. For that reason, people more and more consider seriously the need for a different way to solve disputes, namely when they deal with arcane subject as rights of minority shareholders and corporate law provisions dealing with conflict of interests.

Frankly, I am not totally convinced that specialized courts will solve or significantly reduce this problem: as opposed to what is seen in the United States, at least in the federal judicial system where a judge is appointed for life for a certain post and there is no clear-cut concept of a judicial career, in countries like Brazil judges keep moving from one court to the other, and while one may have specialized courts, there are no specialized judges, who are always advancing towards a more relevant post and, eventually, looking forward to be named appellate courts judges. Thus, the judge of a corporate disputes specialized court will stay there for a couple of years, coming from a specialized tax court and moving to another specialized court, without any actual effectiveness.

On the other hand, while, in common law countries where case law is a relevant concept, and even the lower courts have always the feeling and the pride of being part of the process of creating the law, in civil law countries we see the opposite: more often than not the process of settling a dispute is seen as an *ad hoc* exercise that creates nothing but a solution of a single problem theoretically seen as fair, even at the cost of creating havoc at the whole national legal system.

Moreover, this lack of a true *case law* system causes a general clogging of the judicial system, due to the fact that the very last shareholder or taxpayer out of hundreds of thousands, will be required to go to court on behalf of its own self-interest, causing in many case contradictory decisions and delayed justice, if any at all.

Solving these and other problems is, indeed, the great challenge of civil procedure studies in civil law and, based on my limited knowledge, also in common law countries: after more than a century and a half of an effort, which started in Germany and in Italy and, due in a great extent to the World War exiles, quickly moved to Brazil and other Latin American countries, to form a theoretical system of civil procedure concepts, the sole basic contemporary issues still left open are (i) the effectiveness of the judicial system in order to settle disputes and (ii) how to solve disputes which effects and impacts go well beyond the interest of a determined plaintiff and certain determined defendants which receive service of process.

Indeed, it is simple to refer to the traditional judicial apparatus to solve a landlord-tenant dispute, with the expectation that it will be either fair, as a solution of the dispute, or even if egregiously wrong, will not create any social relevant negative impact but one illegally evicted tenant.

On the contrary, if we deal with a dispute involving the interest of hundreds or thousands or shareholders, civil servants or taxpayers about how to apply a certain provision of the by-laws of a

corporation, of the administrative law or the tax code of a country, the court opinion will in any case generate a ripple effect that may impact thousands of other non-plaintiff or non-defendants.

In other words, we now see disputes that, on the one hand, go well beyond the ability of a normal, or even extremely well prepared judge and, on the other hand which impact will go well beyond the traditional plaintiff-defendant bilateral relationship.

One could say, as a matter of fact, that *private disputes* are less and less *private* and have, in all those cases mentioned above, an inevitable spillover effect that should be taken into account by legislators and by the judicial system, as well as by the parties in drafting contractual provisions that could in the future go sour and generate a judicial dispute.

I must recall having seen, in private practice, cases in which disputed issues have involved arcane issues of game theory or corporate finance, which assume a working knowledge of statistics and calculus (which complete ignorance was a basic requirement to direct a teenager like myself, at least in Brazil, to the study of law).

I have also acted as counsel in other cases, in which the courts had to determine how to construe or interpret contractual provisions that, as a result of the so-called globalization, also relevant as far as drafting of contractual provisions is concerned, were nothing more than poor ( I would rather say *lousy*) translations of English or American standard clauses.

Taking into account this changing context and all these issues and problems, most of them addressed in one way or another, in the morning session, showing that they are not specific of Brazil or of any other developed or developing country, it seems obvious to refer to arbitration and, more generally, to other forms of alternative dispute resolution as meaningful and effective ways to solve this gap between the hardships of reality and the need for effective ways of solving more and more complex disputes.

In this context, as a matter of fact, comparative law tells us that the sole relevant distinction between developed and developing countries is that the latter are facing now issues that were discussed some thirty or forty years ago by the former.

Brazil has recently tried to make up for the lost time, as far as arbitration is concerned: acknowledging the proverbial advantages of arbitration, namely confidentiality, specific knowledge of the arbitrators and rapidity, Brazil recently approved a new arbitration law which, in an interesting historical cycle, goes back to the 1824 Imperial Constitution, which favored arbitration for the solution of private disputes.

For the first time since the enactment of the 1916 Civil Code, the distinction, well-known in civil law countries, between the so-called *clausula compromissoria* – i.e. the theoretical and unenforceable undertaking to arbitrate – and the true and enforceable *compromisso arbitral* was effaced, moving forward a process that had stalled at the 1923 Geneva Protocol, in most nations superseded by the 1958 New York Arbitration Convention, but not in Brazil, which was defined by a well-known French arbitration expert, René David, as an “island of resistance” to arbitration and other forms of alternative dispute resolution.

The most interesting issue in our recent experience was that the strongest resistance against arbitration came from those who, in theory, would benefit most from its adoption: the court system. In Brazil, shooting from the hip, if I may say so, certain judges in their initial opinions, questioned the constitutionality of the new arbitration law. Eventually, the Supreme Court decided, based on precedents from Spain and other countries, that the “right to go to court” was, indeed, a right, and

not an obligation, and therefore those who opted for the arbitration as a dispute resolution mechanism were not deprived of any constitutional rights.

As a result of such ruling of the Supreme Court, Brazil has eventually acceded to the New York Arbitration Convention, as well as it had joined the 1975 Panama Inter-American Arbitration Convention, acknowledging both the validity and the enforceability of arbitral clauses and, more specifically, of foreign arbitration awards in Brazil, an issue oftentimes brought before the Brazilian Supreme Court, with mixed results.

After these relevant stumbling stones on the arbitration path were removed by the Supreme Court and Congress, we are starting to see the reference, if not the actual use of it, to arbitration as an effective solution to private disputes: here and there, more and more private disputes are being referred to either domestic arbitration and, on the institutional front, more and more arbitration chambers are being created, one of which deserves specific attention, being the Arbitration Chamber of the Brazilian Stock Exchange.

Moreover, as you may know, the recently enacted amendment to the Brazilian Corporation Law included a provision<sup>1</sup> whereby the by-laws of a corporation may state that disputes between shareholders and the company, as well as between controlling and minority shareholders shall be finally adjudicated by arbitration.

This creates a new way – while not mandatory in all cases, because mandatory arbitration would most probably be deemed unconstitutional, and therefore dependent upon the adoption of a specific provision in the by-laws of each corporation - to solve disputes between the corporation and its shareholders (either domestic or foreigners, for which purpose there is not distinction), always limited by the general civil law concept that, except when specifically provided, the effects of a final decision will not go beyond the actual plaintiffs in the case.

This provision, by the way, has always restricted the effectiveness of the judicial system in corporate litigation cases, since more often than not the burden of the judicial process would be much higher than the actual benefit that one or a few shareholders would receive.

While we have specific provisions stating that a certain shareholder may act on behalf of all the others, sue the controlling shareholders in something similar to a *derivative suit* and, on the other hand, the *Ministerio Publico* (i.e., the Attorney General) could also do it on behalf of aggrieved minority shareholders, these provisions are seldom seem effective in practice and the general rule is the requirement that each shareholder should act on behalf of himself, which is of course sub-optimal, taking into account a very negative cost-benefit relationship.

Based on this concept, which has already being adopted by a few corporations, the Brazilian Stock Exchange – BOVESPA – inscribed in its *Novo Mercado* regulations a provision whereby this form of settlement of private disputes would be mandatory. Indeed, so far, only a few companies have adhered to either *Novo Mercado* itself or to the so-called *Level 2 of Corporate Governance*, which could be defined as an entry-level to *Novo Mercado* and, in all candor, one could say that the same kind of resistance to the unknown shown by the judicial system is also being evidenced by public corporations.

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<sup>1</sup> § 3º O estatuto da sociedade pode estabelecer que as divergências entre os acionistas e a companhia, ou entre os acionistas controladores e os acionistas minoritários, poderão ser solucionadas mediante arbitragem, nos termos em que especificar.

Once more, this is not new. It happened in Europe in the 30s and in the United States even later, but in our opinion we have gone past the point of no-return and, over time we shall see more and more private corporate disputes being settled by arbitration or, before being actually arbitrated, being subject to a mediation effort.

There are, even now, many other issues to be solved, like whether the adoption of an arbitration provision like the one required by BOVESPA will bind all the shareholders in a public company or whether there will be a grandfather clause for those who want to preserve their right to go to court, or whether an arbitration award granting, say, a certain dividend to some plaintiffs will benefit all the other shareholders or not (an issue, by the way, that remains unsettled also as far as the ordinary judicial system is concerned).

Nevertheless, while not really “polyannic” about the future of arbitration in Brazil, one cannot but acknowledge that it is and in the future will be, more and more, the lesser evil.