Internacional Commercial Arbitration In Latin America: The ICC Perspective

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Arbitrating Corporate Disputes in Latin America

When I read the topic of this panel - Arbitrating Corporate Disputes – it sent me back to year 1850 when Brazilian Commercial Code was enacted.

Such Code was drafted mostly by business people and, of course, to avoid judicial delays and the lack of judge's knowledge of the business practices and its proper and peculiar rules, the old Commercial Code did provide for a compulsory arbitration, inter alia, to solve disputes amongst shareholders.

However, such provision was revoked seventeen years later and, in my opinion, Brazil lost a great opportunity to be ages ahead on this matter.

Nonetheless we have no reason why to be skeptical. Arbitration in Brazil is booming and judicial court's decisions have been very favorable to arbitration and I assume that the Brazilian State Courts will treat positively the topic that I will address: arbitration disputes arising out of the By-Laws of a company.

Whenever such subject matter is approached, the very first question raised by scholars concerns the validity and effectiveness of an arbitration agreement established in the By-Laws of a company by majority of shareholders vote.

The point of discussion stems from the principle of freedom and autonomy of will that shall govern arbitration.

In other words, for a number of law professors, the arbitration agreement inserted in By-Laws shall only be enforced if the general meeting decision is expressly approved by all shareholders of the company.

Hence, in case of absence of any shareholder in the general shareholders meeting or in view of a written opposition to the corporate arbitration clause, those shareholders should not be bound by the arbitration agreement and therefore corporate disputes should, whenever involving them, be solved by State Courts.

But some law professors go further: based on the same consent and autonomy of the will principles, they say that even approved the arbitration clause by a given shareholder, whenever his shares are transferred, the transferee shall expressly agree with the arbitration clause in order to be bound by thereto.

Well, regarding this latter legal position – express approval of the transferee - from my standpoint, this understanding is very conservative and shall not prevail for many legal reasons.

Notwithstanding, the reality is that judicial courts' trend is against such old fashion argument.

In fact, 2 judicial court decisions from the State of São Paulo already disregard such understanding

simply because the transferee assumes all rights, obligations, duties and responsibilities held by the transferor, which includes the content of the arbitration clause.

And, it is noteworthy that the two referred judicial courts decisions not only considered groundless the old fashion argument but also conveyed the parties to arbitrate a dispute that is also subject to debate, that is, the dissolution of the company.

This means that the Brazilian Courts already accepted as arbitrable conflicts involving the dissolution of companies.

So, returning to the very first issue, that is, the submission of all shareholders to an arbitration agreement introduced in the By-Laws by a majority of voting rights, I understand that the relevant point is to interpret the autonomy of the will in connection and in a fine tune with the relevant mandate principles of any corporation.

It is well known that the existence of large corporation is based on 2 essential legal rules: shareholders' limited liability and corporate decisions subject to the majority of voting shares.

These two rules are of paramount importance to the life of a corporation.

It is impossible to admit the flow of a huge amount of capital to a corporation without the limited liability rule and the principle of majority.

These are the two pillars that allow the existence of the corporation in the world.

Therefore, when we bring arbitration rules and concepts onto the scope of corporate law and principles, the autonomy of the will shall be balanced and revisited in view of the relevant rules that govern the existence of a corporation.

And in my point of view, the autonomy of the will is not absolute [e.g. extension of arbitration agreement to third parties] and must not supersede the principle of majority.

Moreover, we should not forget that the rule of majority emerged in France in the beginning of nineteen century exactly to protect the vast minority of the existing shareholders.

So, the rule of majority came into force to avoid or minimize the then existing concentration of powers in the hands of few (the so called aristocratic) and therefore amplify the numbers of corporate decision-makers.

The principle of majority also aligns with the legal nature of the company. Its contractual basis differs from the common ground of most agreements.

What the company By-Laws underline is the joint interest of all shareholders that is, to accomplish the object of the company.

What means, as said by the italian jurist **Vivante**, "A Company (agreement) transform divided individual

rights into a unique and collective interest", the interest of the company.

And to accomplish the unique and collective interest there is no other way than compulsorily apply the rule of majority.

On the other hand, we must have in mind that the voting right is subject to limitation and restrictions, which means that the shareholders are obliged to exercise the voting right seeking always the interest of the company.

A vote shall be deemed abusive if it is exercised with the intention of causing damages to the company or to the other shareholders.

In this sense a question must be raised: does arbitration cause any damage to the company interest or to the shareholders' political or patrimonial rights? I don't think so.

Conversely, it seems that arbitration goes along with company and shareholders best interests.

Corporate disputes have become very sophisticated and shall be solved by experts on the subject.

The general principle is to maintain and keep alive the company to the benefit of its employees, family members, suppliers etc. Therefore, it is quite important to solve corporate disputes on a very expeditious way.

Globalization and high level of competition do not allow management time consuming and changing of focus for a long period of time. Confidentiality is also of essence in intra corporate disputes.

Said that, I do not foreseen any damage either to the company or to any shareholder by means of approving a By-Laws provision whereby disputes involving minority and majority of shareholders or the company and the shareholders shall be submitted to arbitration.

In my point of view, such agreement, approved by a majority of vote, is harmonic and in line with the interest of the company.

Therefore, shall be valid and apply to all shareholders, even to those that have objected the decision took at the general meeting.

This understanding is accepted by most of the Brazilian scholars, even because art. 109 of Brazilian Corporate Law were amended in 2001 to introduce a paragraph 3rd, which provides for arbitration as a mechanism to solve disputes amongst its shareholders or conflicts between the company and its shareholders.

It should be stressed that such provision was inserted in the part of the law that deals with Essential Corporate Rights that neither the By-Laws nor the shareholders general meeting may deprive a shareholder.

And for the sake of understanding, this law provision that expressly accepted corporate disputes being

solved by arbitration did not establish any restriction whatsoever to the insertion of arbitration agreement in the By-Laws of the companies.

It could, for instance, provides for a withdrawal right or a qualified quorum. But it did not! And when a restriction was relevant the corporate legislator did establish it. [1]

Therefore, if the Brazilian Corporate Law authorizes the arbitration to solve intra corporate disputes and no restriction was imposed the majority rule shall prevail.

Although, to the best of my knowledge, no judicial decision has been issued so far in this regard, I assume the trend in Brazil is to judge valid and enforceable a corporate arbitration agreement approved by majority of voting right even because our Stock Exchange – BOVESPA – for more than 5 years imposes the use of arbitration to any company listed in Level 2 of the so called New Market.

Hence, to be listed in Level 2, an outstanding degree of corporate governance, the company shall modify its By-Laws in order to provide for an arbitration agreement.[2]

The arbitration clause to be established in the companies' By-Laws listed in Level 2 of New Market has a very broad scope being applied to solve any and all disputes involving (i) the Brazilian corporate law, (ii) the interpretation and violation of the By-Laws, (iii) the legislation of the Brazilian Securities and Exchange Commission, the rules issued by the Brazilian Central Bank, National Monetary Council legislation and the New Market rules.

Moreover, not only the Companies listed in Level 2 and its shareholders are bound by the arbitration agreement but also the management team and members of the Fiscal Council.

Although some legal controversies may arise out of the legal feasibility of solving Board of Directors' deadlocks by arbitration, in practice we already have in Brazil some deadlocks disputes submitted to current arbitration proceedings.

The legality of such procedure may be back up by art. 129 (par. 2) of Brazilian Corporate Law, enacted in the early 1976, which accepts the possibility of arbitration or a third party decision to solve impairment of a shareholders' meeting decision due to an event of a tie vote.

And this means that, in principle, there is no obstacle in Brazilian legislation to convey to arbitration disputes involving basically business matters.

It is important to highlight this understanding because some scholars advocate that pure business disputes can not be subject to arbitration simply because the jurisdiction exercised by arbitrators has a very clear and specific finality: to apply the iudicium; that is, arbitrators can only decide a conflict by applying the law and therefore are not allowed to decide business issues.

However, in Brazil, as I mentioned, Corporate Law authorizes arbitrators to decide a tie vote event stemming from a general shareholders meeting and our Civil Code establishes that in case of deadlock the issue shall be submitted to a judge decision.

Finally, one word on the arbitration disputes dealing with the right of vote.

Since voting rights are conceptually agreed as a political advantage, someone may raise inarbitrability of the subject matters involving voting right based on the fact that in Brazil art. 1 of our Arbitration Law says that only “disputes related to freely transferable patrimonial rights” are subject to arbitration.

In this particular I understand that the vote is a legal mechanism granted to the shareholder to participate and influence the company’s activities, productivity and efficiency; the voting right seeks to improve company’s profitability and the optimization of the shareholders investment; companies are set up to be profitable and distribute resources to its shareholders.

In other words, matters involving right of vote or related issues, in my opinion, may be subject to arbitration simply because, at the end of the day, the purpose envisaged by shareholders when exercising such right is to protect and enforce their patrimonial rights.

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Endnotes

1 For instance, article 36 establishes some possible limitations on transfer of shares.

2 Note that approximately 60 large companies are listed therein.