

Brazil set for wave of derivative litigation?

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Brazil's finance lawyers are divided on whether the country will see a surge in lawsuits following a series of high-profile derivative losses by some of the country's leading companies.

The country's second largest food company Sadia already faces a US court action over allegations that it misled shareholders over currency hedging, while a similar class action has been filed against paper and pulp company Aracruz. Some Brazilian lawyers think that companies in turn may take action against the banks that sold and advised them on their derivative investments.

Marcelo Freitas Pereira, a partner of **Siqueira Castro - Advogados** says, "A wave of litigation is expected, with great sums involved."

He explains, "We have been consulted by several clients and prospective clients about issues in connection with derivatives. The advice we give is: to look deeply inside and identify the root of the issue, assess the losses, evaluate whether it is possible and/or feasible to push a stop-loss provision, consider and prepare damage control to protect managers from shareholder claims, take action to resolve the issue, and evaluate whether litigation (or arbitration) is the best route to resolve the issue."

Edmundo Nejm of Lefosse Advogados is also expecting to see a rush of lawsuits, but points out that the leading law firms might choose not to take part. "Litigating against banks will be difficult for larger firms and there should be a surge of smaller firms which will specialise in this type of litigation."

He thinks that the cases are likely to come from insolvent companies, as those with any hope of continuing business will try to avoid fighting with their banks. "It does them no good in the longer term to cut relationships with those institutions most active in the relevant markets. Who else will deal with them if they don't pay their obligations?" he adds. "All bets are off where there is a bankruptcy."

José Augusto Martins of Trench, Rossi e Watanabe Advogados agrees, pointing out that courts are likely to take the high risk involved in derivative betting into account when hearing cases brought by investors.

"In these cases, we would most likely advise clients to negotiate the issues rather than commencing immediate litigation," he says. "In the current circumstances, and where the agreement clearly says that heavy losses could be part of the deal, litigation could bring even more losses."

And Freitas also believes some companies must share a portion of the blame for their own losses. "The irresponsible credit exuberance in past years has led a great number of companies to either neglect the proper risk assessment upon entering on a derivative contract, or believe that they could bet with derivatives like a casino blackjack. Since we have had a global boom recently, the risks associated with derivatives were swept under the carpet and only just come to the surface," he says.

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