



# PETROBRAS LITIGATION RESEARCH REPORT & POINT OF VIEW

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## Petróleo Brasileiro S.A. (Petrobras) (PETR3, PETR4)

### Court Hands Down Strong Ruling in Favor of International and Brazilian Petrobras Shareholders and Bondholders, suffering Petrobras Stock Price (PETR3 PETR4) and Certain Bond Price Losses from the Lava Jato Scandal

**On May 26, 2021**, after several years of litigation, the District Court in Rotterdam in the Netherlands came down with a ruling indisputably in favor of international and Brazilian shareholders and certain bondholders suing Petrobras for wrongdoing and economic losses suffered in connection with the infamous “Lava Jato” scandal.

Petrobras previously settled a similar case for USD \$3 billion with a sub-set of shareholders buying shares via US ADRs on the NYSE and investors buying USD denominated bonds. The much larger class of international and Brazilian shareholders who bought shares directly on the primary Brazilian B3 exchange in Sao Paulo, and a smaller class of bond holders, have thus far been left behind with no resolution for their losses.

In January 2017, the Dutch Stichting Petrobras Compensation Foundation (SPCF), supported by international investors from more than 14 countries and a coalition of funders and lawyers, commenced litigation against Petrobras in the District Court of Rotterdam in the Netherlands. Except for the Brazilian Government and its agencies, the US ADR and bondholder settlement class, and shareholders that opted to go to arbitration or litigation in Brazil, the SPCF universally covers the interests of all other remaining international shareholders, Brazilian shareholders and a smaller group of certain non-USD denominated bondholders.

The SPCF shareholder class is estimated to be around 50% larger than the US ADR class that settled for USD \$3 billion. During the US lawsuit, experts estimated the actual damages for US ADR investors exceeded USD \$10 billion. Accordingly, the US settlement provided a cash payout to participating ADR holders of approximately 32.7% of their total damages after legal, court and administration fees.

In comparison, the SPCF shareholder class includes investors with estimated potential damages near \$15 billion. While damage calculations in themselves are complex, it is telling that Petrobras’ own company reports during the relevant period charts the Brazilian government and agency holdings to be a little under half of the company’s shares, with the remaining shares split approximately 40% to US ADR holders and 60% to international and Brazilian shareholders. This high-level picture gives us some comfort that the comparable estimated (\$10/\$15 billion) damage assessment between the US litigation and the Dutch litigation is somewhat meaningful.

#### **What we believe the May 26, 2021 ruling is about and what we believe it could mean**

While the litigation in the Netherlands has somewhat gone under the radar with the public and market analysts, this new ruling should sound an alarm for all interested parties. Petrobras’ potential exposure to liability has increased significantly.

The Dutch litigation involves allegations of Petrobras’ bribery of government officials, contractors, and others, together with other fraudulent actions and compliance breaches.

Petrobras agreed not to dispute similar charges in the United States, where it [entered into a Non-Prosecution Agreement \(“NPA”\) with the U.S. Department of Justice \(DOJ\)](#). In the Statement of Facts accompanying the NPA, DOJ cited several violations of the Foreign Corrupt Practices Act (FCPA) as well as violations of shareholder disclosure regulations under the Sarbanes Oxley Act. To resolve the charges against it, Petrobras agreed to pay a \$853.2 million criminal penalty to U.S. and Brazilian authorities and agreed to adopt significant remedial actions regarding Board management, control, and compliance; it separately entered into a \$3 billion class action civil settlement with US American Depository Receipt (“ADR”) investors. Now that the Dutch litigation has moved past preliminary battles over jurisdiction and standing, the case will focus on whether the allegations of bribery, fraud, and corruption are true, whether Petrobras’ actions violated applicable laws in the Netherlands, Brazil, and other select jurisdictions, and what damages the international and Brazilian investors suffered as a result of Petrobras' conduct.

SPCF began corresponding with Petrobras in 2016 and ultimately proceeded to file an action on January 23, 2017. Since the action started SPCF has overcome numerous challenges from Petrobras. Some of the main battleground issues have been Petrobras’ attempts to challenge:

- Whether a foundation, the SPCF, supported by Petrobras shareholders could sue in the Netherlands
- Whether the SPCF in fact had support of a diverse representative section of shareholders
- Whether the SPCF had standing to sue
- Whether Brazilian Portuguese speaking shareholders or international shareholders represented by Portuguese speaking intermediaries, should be excluded from the lawsuit

After five years of active litigation and hundreds of pages of court briefs, responses, expert reports, oral hearings and rulings, we believe the May 26, 2021 ruling clearly sums it up. From our research we believe, and as further confirmed to us in conversations by Dutch lead counsel in the case, Lemstra Van der Korst N.V. and other outside legal counsels following the matter, that the key points of the rulings are:

- SPCF has legitimate standing and can sue Petrobras “in Dutch courts” on the “merits” of the case. The Court wholly rejected the Petrobras Defendants’ argument that the Petrobras investors who purchased shares on the B3 and linked markets in the EU have no right to seek relief in the Netherlands pursuant to article 58 of the Petrobras Articles of Association – the so-called Petrobras arbitration clause. (We understand the merits mirror the bribery and fraud allegations that Petrobras has already admitted to in their DOJ settlement and that has subjected them to criminal and securities violation charges in other jurisdictions.)
  - The Court in Rotterdam took particular issue with the disingenuous attempts by Petrobras to advance the argument for the arbitration requirement in the Rotterdam Court when, in fact, the same Defendants argued the exact opposite in arbitration proceedings in Brazil – a contradiction for which SPCF provided evidence to the Court during the most recent oral hearings held in Rotterdam in January 2021.
  - The Court also noted how a broad interpretation of the arbitration clause would result in the shareholders being denied access to an independent national court. Since access to an independent court is a fundamental right, any provisions in the articles of association that would cut off this route should be clear and unambiguous. The Court determined that this was not the case since Brazilian courts have ruled on two occasions that article 58 of the Articles of Association only applies to the internal operations of the company. Since SPCF's case did not concern a dispute about the internal operations of the company, the Court ruled that the arbitration clause did not apply.



- International shareholders and Brazilian shareholders, whether Portuguese speaking or represented by Portuguese intermediaries, are not excluded from the class. The facts presented by SPCF resulted in the Court reversing its earlier interim ruling on the interpretation of article 58 of the Articles of Association and affirmed the SPCF's position that the class of Petrobras investors should include all eligible investors and not exclude a subset of investors, whether Portuguese speaking or represented by Portuguese intermediaries.
- The Court ruled that Petrobras investors who are currently actively engaged in arbitration proceedings or separate litigation for the same facts in Brazil or elsewhere are excluded from the global class of investors for whom SPCF in the Netherlands litigates.
- The Court affirmed that SPCF represents a sufficiently large class of investors and that the collective action process in the Netherlands is an efficient vehicle by which to prosecute the claims of the eligible and damaged class of global investors.
- The Court set a date of September 1, 2021 for SPCF to submit its further arguments and facts regarding the merits of the case and specifically the arguments that support SPCF's allegations that Petrobras violated investors' rights under applicable laws as previously determined by the Court in Rotterdam.

## Point of View

### Jurisdiction

When originally researching shareholder and investor options for recourse, we were concerned with the suggested Brazilian arbitration route. It seemed for this matter there were several inherent conflicts of interests, that could potentially impose undue influence on the outcome. Among other things, the Brazilian government collects billions of dollars in oil concession fees from Petrobras and it is a lawmaker with voting control and ownership of about half of the company. The legal issues in this case, far exceed the scope of the typical matters (trading or listing violations) an exchange arbitration panel would be equipped to deal with. We have always believed that the serious allegations and nature of the fraud and criminal violations were better suited for civil and criminal courts.

It made sense that SPCF should seek redress in a neutral forum. We always were convinced that there was more than sufficient nexus to sue Petrobras in the Netherlands. Petrobras Global Finance B.V. is headquartered there and it is a key location for its international operations with other Petrobras subsidiaries located there as well. Further, Dutch companies have been involved in anti-corruption investigations and regulatory settlements involving Petrobras.

In 2010, Petrobras established linked-market trading access to its shares via European exchanges, such as the Spanish Bolsa Madrid. The move was a part of its agenda to attract international investors and present itself as a true global company. In doing so, Petrobras became subject to compliance with the local policies and regulations, implemented by the various linked exchange and EU based financial markets regulators.

Ultimately, it was the combination of various legal technical issues around the above jurisdiction and standing issues that resulted in the ruling handed down last week.

It is most notable, that during the SPCF litigation in the District Court in Rotterdam, Petrobras argued that investors should not be allowed to sue in the Netherlands. Instead, Petrobras argued that shareholder rights under the Company's Articles of Association must be enforced in arbitration at the Market Arbitration Chamber (CAM B3) at the Brazilian B3 stock exchange in Sao Paulo. It appears that argument went down in flames, as it surfaced that Petrobras in parallel have been legally resisting or rejecting investors pursuing arbitration in Brazil, arguing the arbitration clause was too narrow to also cover shareholders losses following the Lava Jato scandal. In arguing opposite positions in the Netherlands and Brazil, Petrobras apparently tried to create a legal vacuum with nowhere to go for investors. The Dutch court wouldn't have it.

Petrobras has deployed significant litigation resources in Rotterdam District Court to avoid at all costs the rulings handed down by the Dutch judges and situation that has now arrived. While some of Petrobras' arguments may be considered by some observers as slippery and smoke and mirrors, the Court's decision cut through the issues and leaves no ambiguity.

Impacted shareholders can be pleased that the Dutch forum has proven to be a proper, qualified and objective forum; free of the inherent conflicts of interest that exists in Brazil.

### **Understanding international and Brazilian B3 Shareholders vs ADR holders in this context of this litigation.**

Traditionally, investors trade shares directly on the "home" or primary exchange where a company, in this case Petrobras, is listed. However, in the US, it is sometimes possible to buy ADRs – American Depositary Receipts for certain companies' shares. As the word "Receipt" indicates, it is not an actual share, but a receipt for a share or number of shares in a company. In the case of Petrobras, one ADR represents a Receipt for two Petrobras shares. The ADRs trading on the NYSE in the US are quoted in US Dollars and the "underlying" shares are issued in Brazilian Reais. An ADR receives dividends generated from the underlying shares and the holders have the right to vote the underlying shares. For the amount of ADRs traded, a custodian, in this case JP Morgan, must keep in custody the corresponding amount of underlying Brazilian shares. While those shares do not typically circulate in the free float, they are the exact same type of shares as those circulating in the free float. In fact, and while unusual, an ADR holder could ask to exchange the ADRs for the underlying shares. ADRs are typically purchased by US domiciled investors or dollar-based investors, who prefer the convenience of trading in dollars with the custodian converting dividends into dollars.

In light of the above explanation, it is clear there is absolutely no difference between free float shares and the underlying ADR shares held in custody by the sponsoring custodian.

This fact is important when comparing shareholder damages and the settlement resolution already achieved in the US Petrobras litigation versus the potential damages and potential discussions about settlement resolution in the Dutch international litigation.

Why has Petrobras paid \$3 billion to one group of damaged shareholders in a settlement and not the other? Both groups own the exact same share directly or indirectly, with the same value, dividend and voting rights. One could argue that the US ADR settlement amounts to a form of shareholder discrimination, as Petrobras essentially provided the equivalent of a "special dividend" to one select group of damaged shareholders, at a high cost to the remaining group of damaged shareholders that received nothing (to date). In fact, the investors that fall outside the scope of the US settlement are harmed twice. First, the Lava Jato fraud itself was damaging to shareholder value, and second, Petrobras is withholding compensation handed out to other shareholders. Not only legal, but also fundamental fairness and political issues are at stake when a company favors shareholders trading shares on a US exchange, rather than the home and primary exchange of the company.

To be clear, there is no obstruction preventing Petrobras from treating all investors equally. It is true Petrobras have argued that investors participating in the US ADR and bond settlement under the US settlement agreement are barred from suing them in other jurisdictions. But our read of the US settlement agreement leaves little doubt that shares traded on the B3 are explicitly exempt from this restriction and the scope of the release.

In all events, we believe the overlap between traditional investors transacting in both ADRs on the NYSE and the direct shares on the B3 exchange in Sao Paulo is rare, for logical reasons. For instance, it would make absolutely no sense for a Brazilian investor to buy ADRs and go through the cost and spread on forwards and back currency transactions on purchase, sales and receipt of dividends or dealing with the hassle of voting the shares via a US custodian.

## What Happens Next

### Litigation

The Court has set a date of September 1, 2021 for SPCF to submit arguments and facts in support of the merits. The Court stipulated that the Petrobras defendants would have three months from September 1, 2021 to submit its defense to SPCF's allegations. An oral hearing will be scheduled once the Court has received all the parties' briefs. It is estimated that the oral hearing will be scheduled for mid-year 2022. At the oral hearing, both parties will have the opportunity to submit additional evidence before the Court renders a final ruling on the merits of the case, potentially – "Declaratory Relief" (Declaratory Relief is in essence a "ruling on wrongdoing"). Upon a favorable ruling for the investors and clearance of any appeals, the litigation will proceed to the damages phase, where investors can sue for full damages and interest.

Given recent legal developments that confirm SPCF's standing to sue in the Netherlands, and Petrobras' prior admissions in the Lavo Jato scandal, the facts and odds do not appear to be in Petrobras' favor.

### Damages Assessment

Total actual damages for US ADR investors were estimated by experts to exceed USD \$10 billion. We believe the SPCF represents international and Brazilian shareholders with an estimated amount of damages near \$15 billion. This number does not account for bondholders, which also have significant damages.

This estimate may sound high. In our view, it is however entirely proportionate, relative to the large amount of cash Petrobras had convinced investors to invest, and relative to the drop in share and bond prices resulting from the Lava Jato scandal.

It is important to remember that ahead of the scandal, Petrobras was doing elaborate international share offerings and set a world record in a single offering, when raising an additional \$70 billion from equity investors in 2010. The Company deliberately established linked market access arrangements with European stock exchanges and conducted extensive "Road Shows" across major European cities, to access many investors there. In addition, at the time it also had also raised a staggering amount of more than \$100 billion in cash from bond sales to international investors.



Reasonable minds can differ on whether the US settlement of \$3 billion was fair or simply a “parking ticket” against the approximately \$10 billion ADR investors lost there. Indeed, some Wall Street analysts were surprised that the \$3 billion settlement in the US, while large by securities class action settlement standards, was not settled for an even greater amount. But in all events, the US settlement never addressed the much greater class of losses. So, the elephant in the room, remains the enormous loss suffered by international and Brazilian investors who traded directly in the open market on the primary exchange in Brazil and were unable to benefit from the US settlement.

Some experts have independently studied the Dutch litigation related investor damages through comprehensive “event” and “damage” studies. Examining the information, we believe the result is pretty much the same, whether you make an apples-to-apples comparison with the US litigation damages or you look at a separate independent damages study of the shareholder and bondholder losses at issue in the Dutch litigation.

### **Judgement or Settlement**

In almost 99% of all US class actions and most collective actions, the parties choose to settle once the writing is on the wall. The risk of an all-out loss with interest, is simply too great of a gamble for the issuer, in this case Petrobras.

We believe that a Declaratory Relief ruling for shareholders would not only generate extensive damages litigation and financial exposure for Petrobras, but it would also complicate corporate risk assessment, credit ratings, disclosures and relations with investors and capital markets.

Of course, in the absence of a settlement, SPCF and the Petrobras investors belonging to the class would pursue litigation for full damages, greatly assisted by a Declaratory Relief ruling.

Generally speaking, for a defendant, any settlement discussion is naturally better before a potential Declaratory Relief ruling and much worse after the ruling, assuming it goes against them. A Declaratory Relief in a European Union based court seems quite possible, considering Petrobras has already stipulated to (or conceded to not dispute) wrongdoing in their Non-Prosecution Agreement with the US Department of Justice.

In all events, it will be very interesting to follow.

### **About**

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The Company’s analysts and experts have distilled content, collected and performed statistical outcome analysis across several thousand litigation cases, settlements and settlement implementations.

The Company is actively tracking all current litigations and settlements. Combining academic and seasoned practitioners expertise in financial market operations, market structure, trading, economics, finance with significant insight and research of litigations and settlements, Battea Global Litigation Research Inc., is one of the world’s most proficient analysts within its field.

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References in this report to allegations of Petrobras' bribery of government officials, contractors, and others, together with other fraudulent actions and compliance breaches, and to Petrobras' violations of applicable laws in the United States, Netherlands, Brazil, and other jurisdictions, are based on court filings in the United States and Netherlands and on publicly available information on government and third-party websites. Until proven in a court of law or admitted to by Petrobras, these are merely allegations of fact and do not represent an adjudication on the merits.

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Shareholders and investors that wish to participate in any potential recovery from a settlement, litigation or otherwise should directly contact ISAF Management Company, the administrative, marketing and funding firm selected by SPCF:

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**INFORMATION LINKS:**

**DOJ/SEC Source Material**

- DOJ press release on \$853 million criminal penalty: [Click here to learn more.](#)
- DOJ Non-Prosecution Agreement: [Click here to learn more.](#)
- SEC settlement order: [Click here to learn more.](#)

**Petrobras Issued Source Material**

- Petrobras Investor Relations Website with annual reports and 20F source material on share ownership – the presentations are not consistent across the years with some info reported in 20Fs and some in Management Reports for the corresponding years: [Click here to learn more.](#)
- Petrobras 2014 Management Report (page 5 of 94 for Ownership Structure): [Click here to learn more.](#)
- Petrobras 2015 20F – the Management Report is not available to download on the website, so no section on Ownership Structure (page 135 of 309 for Major Shareholders including ADRs): [Click here to learn more.](#)
- Petrobras 2016 20F – the management Report is not available to download on the website, so no section on Ownership Structure (page 141 of 405 for Major Shareholders including ADRs): [Click here to learn more.](#)
- Petrobras 2017 Management Report (page 54 of 135 for Ownership Structure): [Click here to learn more.](#)

**Dutch Court Documents**

- English translation of May 26 ruling. The ruling has been redacted to blind identities of natural persons as required by Dutch privacy laws. [Click here to learn more.](#)