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# **GLOBALIZATION OF SECURITIES ENFORCEMENT: A SHIFT TOWARD ENHANCED REGULATORY INTENSITY IN BRAZIL'S CAPITAL MARKET?**

*Eugenio J. Cárdenas\**

## INTRODUCTION

As we are constantly being reminded, capital markets are now so globalized and highly interconnected that a weakness within one market or within its regulatory oversight can serve to undermine other markets, like a weak link in a chain . . . . Our partnerships with regulators throughout the world are critically important to rooting out fraud and misconduct in our markets . . . . Over the years . . . we all have come to reach a better understanding of how critical it is—especially in a fast

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This Paper was prepared for the “Globalization of the United States Litigation Model” symposium, co-sponsored by the Dennis J. Block Center for the Study of International Business Law at the Brooklyn Law School, and by the Brooklyn Journal of International Law (Brooklyn Law School, October 21, 2011). Special thanks go to Professors Arthur Pinto and James Park, from Brooklyn Law, for “discovering” my scholarship and kindly inviting me to participate in the Symposium. I am deeply grateful to Maria Helena dos Santos Fernandes de Santana, Chair of Brazil’s Securities and Exchange Commission (“CVM”), and of the International Organization of Securities Commissions’ (“IOSCO”) Executive Committee, and to Alexandre Pinheiro dos Santos, CVM’s Attorney General, for providing their invaluable insight and support during the ongoing elaboration of this project and helping me understand and convey this “story” about Brazil’s recent experience with securities enforcement. I thank Z. Scott Birdwell, Branch Chief for Technical Assistance and Special Counsel for Enforcement in the Office of International Affairs, U.S. Securities and Exchange Commission (“SEC”), for sharing—while still unpublished—his scholarly work on securities enforcement, namely his “Roadmap for Emerging Markets,” employed as a model in this paper to assess Brazil. The article greatly benefited from comments by SEC Commissioner Troy A. Paredes, Professor Michael Klausner, Professor Stephen H. Haber, Professor Deborah R. Hensler, and participants of the Globalization of the United States Litigation Model Symposium (Brooklyn Law School, October 21, 2011), the Yale Law School Doctoral Scholarship Conference (Yale Law School, December 2–3, 2011), and the Stanford Law School JSD Research Colloquium (Stanford Law School, January 17, 2012). I kindly dedicate this paper to my newborn son, Eugenio Cárdenas Handal, hoping that someday it may be of his interest. The views expressed here are my own and do not necessarily reflect the views of the SEC, its officials, or its staff, where I worked during the Fall of 2011 when I wrote this Article.

moving global marketplace—to . . . learn . . . best practices from around the world that we can incorporate, as appropriate, into our respective enforcement programs. This sharing of best practices results in a race to regulatory quality as opposed to the proverbial race to the bottom. It is my hope, and belief, that such a race to the top will create real benefits for investors in the markets under our jurisdictions.<sup>1</sup>

The above words, recently conveyed by U.S. SEC Commissioner Elisse B. Walter to her counterpart regulators from over sixty jurisdictions of the world, echo the increasing phenomenon of global legal convergence and international cooperation among securities commissions, in the realm of capital market surveillance and enforcement. This Paper, written for the “Globalization of the United States Litigation Model” symposium at Brooklyn Law School, October 21, 2011, ventures into the mentioned phenomenon, to explore the following puzzle of globalization, corporate law enforcement, and financial development—are emerging capital markets shifting toward enhanced regulatory intensity in the enforcement of their securities laws, under the context of global legal convergence?

In that spirit, focus is placed on the emerging Latin American region, namely Brazil’s securities market. Aim is set at identifying and reflecting upon selected instances that, when combined and analyzed, suggest that Brazil has pursued the enforcement of its securities laws with enhanced regulatory intensity during the past decade—both in terms of adopting enforcement practices characteristic to developed global markets, and of implementing these practices—in light of preliminary evidence of enforcement on the ground.

By the turn of the century, Latin America had undergone an unprecedented democratization wave<sup>2</sup> accompanied by a period of “intense and growing commercial and financial exchange among countries” usually referred to as globalization.<sup>3</sup> As with other contemporary democracies, countries of the region became tied to the “rule of law,” which typically

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1. Elisse B. Walter, Comm’r, U.S. Sec. & Exch. Comm’n [S.E.C.], Remarks at the Closing of the U.S. SEC International Institute for Securities Enforcement and Market Oversight (Nov. 18, 2011), *available at* <http://www.sec.gov/news/speech/2011/spch111811ebw.htm>.

2. See LARRY DIAMOND, *THE SPIRIT OF DEMOCRACY: THE STRUGGLE TO BUILD FREE SOCIETIES THROUGHOUT THE WORLD* 41 (2008). Diamond refers to a third wave of democracy, before the turn of the century, which includes Latin America.

3. Lawrence M. Friedman & Rogelio Pérez-Perdomo, *Latin Legal Cultures in the Age of Globalization*, in *LEGAL CULTURE IN THE AGE OF GLOBALIZATION* 1, 4–5 (Lawrence M. Friedman & Rogelio Pérez-Perdomo eds., 2003).

involves stable rules, honest judges, enforcement of contracts, and a reliable civil service.<sup>4</sup> Further, convergence among legal systems quickly spread across Latin American securities markets. In this legal convergence process, the enforcement of corporate law gained particular relevance for its potential to ensure higher disclosure and governance standards aimed at investor protection and capital market development.<sup>5</sup>

Driven by this global convergence phenomenon, a discourse on “financial regulatory intensity”<sup>6</sup> was triggered within the United States (“U.S.”) law and finance literature. Building on theories advancing that the enforcement of corporate law fosters investor protection,<sup>7</sup> and, in turn, capital market development,<sup>8</sup> and economic growth,<sup>9</sup> this discourse seeks to determine the intensity with which jurisdictions should enforce their financial regulations. Conceptually, optimal regulatory intensity may be thought of as enforcement that is enough to deter, and/or compensate,<sup>10</sup> or when considered from a cost-benefit analysis, as an assessment of whether the marginal benefits exceed the marginal costs of additional enforcement. Despite these conceptual views, there is no clear empirical measure of optimality or levels of enforcement. Nevertheless, significant efforts have started to present preliminary evidence of enforce-

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4. *Id.* at 16.

5. Securities enforcement has, for example, been a recurring theme in The Latin American Corporate Governance Roundtable meetings for over a decade. Among other efforts, the roundtable has applied a series of surveys aiming at better understanding the regulatory and institutional frameworks of the main securities enforcement systems of the region. Regulators, policy-makers, and market participants gather on an ongoing basis to discuss these surveys’ results, and other developments.

6. See John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229, 229–78 (2007) [hereinafter Coffee, *The Impact of Enforcement*]; Howell E. Jackson, *Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications*, 24 YALE J. ON REG. 253, 275 (2007).

7. See Rafael La Porta et al., *What Works in Securities Laws?*, 61 J. FIN. 1, 27–28 (2006) [hereinafter La Porta et al., *Securities Laws*].

8. See Rafael La Porta et al., *Law and Finance*, 106 J. POL. ECON. 1113, 1114 (1998) [hereinafter La Porta et al., *Law and Finance*]; Rafael La Porta et al., *Legal Determinants of External Finance*, 52 J. FIN. 1131, 1131–32 (1997) [hereinafter La Porta et al., *Legal Determinants*]; Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 738 (1997).

9. See Robert King & Ross Levine, *Finance and Growth: Schumpeter Might Be Right*, 108 Q.J. ECON. 717, 717–18 (1993); Ross Levine & Sara Zervos, *Stock Markets, Banks, and Economic Growth*, 88 AM. ECON. REV. 537, 537–58 (1998).

10. See Andrew Kuritzkes, *Section V: Sarbanes-Oxley Section 404*, in COMM. CAPITAL MKT. REG., INTERIM REPORT OF THE COMMITTEE ON CAPITAL MARKETS REGULATION 115 (Jenepher Moseley ed., 2006) [hereinafter INTERIM REPORT], available at [http://www.capmktreg.org/pdfs/11.30Committee\\_Interim\\_ReportREV2.pdf](http://www.capmktreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf).

ment in action that speaks to the intensity with which markets enforce their corporate law, providing a better understanding of securities enforcement systems and their benefits across jurisdictions.<sup>11</sup>

This Paper addresses Brazil, the leading Latin American financial system. It looks into its securities enforcement system during the wave of legal and institutional reform dating back to the turn of the century,<sup>12</sup> resulting from competing dynamics between incumbent controlling owners resisting change, and global forces demanding enhanced corporate law and governance.<sup>13</sup> A decade onward, the study attempts to identify whether Brazil's capital market shows signs of enhanced regulatory intensity in the enforcement of its securities laws.

To approach this question, this Paper queries into the extent to which Brazil has (1) adopted a more robust institutional design of enforcement, and (2) boosted its implementation. To that end, the research identifies and reflects upon selected accounts that suggest enhanced enforcement structures and powers, and increases in actual enforcement activity and resources allocation toward enforcement during the past ten years.

Among other findings, this study identifies a transformation of Brazil's securities enforcement system, both in the establishment and implementation of new institutions and enforcement practices and the revival of old ones. This evolution followed a shift in policy in 2005, whereby Brazil's Securities and Exchange Commission (Comissão de Valores Mobiliários—"CVM") decided that securities enforcement was its main priority.<sup>14</sup>

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11. See John Armour et al., *Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States*, 6 J. EMPIRICAL LEGAL STUD. 687, 689 (2009); Jackson, *supra* note 6, at 278–86; Howell E. Jackson & Mark J. Roe, *Public and Private Enforcement of Securities Laws: Resource-Based Evidence* 11 (Harv. Univ. Law Sch. Pub. Law & Legal Theory Research Paper Series, Paper No. 08–28, 2009), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1000086](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1000086).

12. See Maria Helena dos Santos Fernandes de Santana, Chair, Comissão de Valores Mobiliários [Brazilian Securities & Exchange Commission] [CVM], Presentation at Foro Sobre Modelos de Supervisión: Evolución de la Regulación de los Mercados de Valores en Brazil (Sept. 16, 2008) (Braz.).

13. See Ronald J. Gilson, Henry Hansmann & Mariana Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the U.S. and the EU* 45–46 (Eur. Corp. Governance Inst. [ECGI] Working Paper Series in Law, Paper No. 149, 2010), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1541226](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1541226). Gilson et al. discuss how resistance to corporate governance legal reform, by incumbent players of Brazil's financial system, led to the establishment of the Novo Mercado market that, via self-regulation, imposed standards that went beyond the law.

14. CVM's prioritization on enforcement began with the administration of former Chair Marcelo Trindade, and deepened under the responsibility of current Chair María

CVM appears to be evolving into an ex-post enforcement-driven agency. Somewhat like enforcement systems in developed markets, such as the U.S. Securities and Exchange Commission (“SEC”) model, Brazil’s regulator now embeds features like a Board of Commissioners with political independence, a stand-alone enforcement program with a mandate, an enhanced tool-kit to combat serious wrongdoing, the possibility to negotiate settlements, and partnerships with the criminal justice authorities, the industry, and the international community.

Developments suggesting enhanced regulatory intensity include CVM’s new enforcement program. Through specialized divisions—the *Superintendencia de Processos Sancionadores* and the *Procuradoria Federal Especializada*—this program introduced a new institutional design, combining CVM staff with federal attorneys and investigators. The latter half of the decade accordingly saw an increase in enforcement activity in terms of administrative actions and sanctions pursued and imposed by this new enforcement program. Also notable was the significant reduction in the time required to decide even the most complex administrative procedures. Moreover, serious wrongdoing, namely insider trading and market manipulation—which had been criminalized earlier in the decade—began to be more visibly targeted and sanctioned, not only administratively, but also through an older institution that had seldom been employed—the Collective Civil Action. A strong partnership with the criminal justice authorities also grew, capitalizing on the mentioned offenses. Tools for “real-time” enforcement, including the freezing of assets, subpoena powers, and injunctive orders, began to be deployed as well.

Additionally, the Committee for Settlements of Proceedings was established by CVM in order to identify and propose potential settlements and institutionalize the settlement negotiation process. Consequently, the latter half of the decade saw a striking rise in *Termos de Compromisso* settlements, an instrument that had been available to the regulator for years but that lacked legitimacy and use.

Revealing signs of a “multiple-enforcers” model, an enhanced Self-Regulatory Organization (“SRO”) regime developed in both mandatory and voluntary fronts. On the statutory—thus, mandatory—dimension, CVM provided for a detailed legal framework of self-regulation for or-

ganized markets<sup>15</sup> that not only resulted in enhanced listing requirements, but also in practically outsourcing market surveillance to an autonomous non-profit organization with enhanced rule-making and enforcement powers, *BM&FBOVESPA Supervisão de Mercados* (“BSM”). On the voluntary front, the regulator provided incentives that resulted in firms listing in the market segments of the stock exchange that require higher corporate governance standards, including the Novo Mercado market.

Cooperation with other securities regulators, adherence to international principles, and sponsoring technical assistance workshops for improving enforcement, led by developed markets, became clear trends, too. The increase in enforcement activity was supported by a surge in budget and staffing resources during this period.

Perhaps the biggest hurdle faced by Brazil’s securities enforcement system is in the private enforcement arena. The lack of specialized tribunals and judges trained in capital market matters has resulted in costly and stagnant procedures and in the practical nonexistence of private rights of action. There are, nonetheless, signs of judicial specialization, with an experiment involving a commercial court. In addition, communication and information and knowledge exchange regarding capital markets has increased between the regulator and the judiciary. CVM and the judiciary have made agreements to that effect, whereby the judiciary increasingly resorts to CVM for technical support on securities regulation.

These research findings showcase how a new corporate governance culture is permeating the Brazilian securities market, reshaping legal structures and institutional designs of enforcement in the global arena. The findings provide a story about how emerging global markets may shift toward enhanced enforcement as they become aware of its potential benefits for their development. Finally, they shed light on how legal systems undergo transformation, in view of the interplay between social change, legal cultures, and institutions.

Among other sources, the research draws from assorted data on enforcement activity and resources made available by CVM, published by its Ministry of Finance, and reported by the Latin American Corporate Governance Roundtable for Corporate Governance throughout the decade. Interviews with CVM’s Chairperson, and its Attorney General, offer a reaction to the data, further illustrating the development and challenges of securities enforcement in Brazil.

The Paper unfolds as follows: Section I comments on the financial regulatory discourse and the potential benefits of securities enforcement,

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15. Including over-the-counter (“OTC”) and commodities and futures markets.

with a focus on Latin America. Section II identifies and comments on particular accounts of legal and institutional reform in Brazil's securities enforcement system during the past decade. It further discusses how this framework has been implemented, in light of preliminary evidence of enforcement activity. The Article then presents concluding remarks on how these newly adopted institutions and their implementation reflect enhanced regulatory intensity.

### I. A WORD ON FINANCIAL REGULATORY INTENSITY AND THE PERCEIVED BENEFITS OF SECURITIES ENFORCEMENT IN LATIN AMERICA

Was there reason to believe that the emerging markets of Latin America would develop enhanced regulatory intensity in the enforcement of their securities laws by the end of the past decade? At the turn of the century, the answer might have likely been negative. Globalization, the rule of law, and legal convergence started to surface at the time in the region's securities markets. Countries joined the Organisation for Economic Co-operation and Development ("OECD") and, consequently, issued corporate governance codes. Best corporate practices even found their way into the formal legal systems of the region.<sup>16</sup> Yet, it would have been hard to believe that the incumbent players of the securities markets would give up their private benefits of control<sup>17</sup> and, in turn, give in to corporate governance, minority rights, and investor protection. It would have been difficult to imagine that strong regulatory frameworks governing the public firm would arrive and then be implemented and enforced effectively. After all, it remained highly questionable as to whether the basic preconditions of a strong capital market—property and contractual rights and their enforceability—were even in place.

Despite the region's historical reputation for being a difficult corporate environment,<sup>18</sup> investor protection ultimately gained considerable rele-

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16. For example, as early as 2001, the Mexican Securities Market Law was reformed, introducing substantive corporate governance provisions that were originally in the voluntary Best Corporate Practices Code. This tendency followed with reforms to the same law in 2003 and with the creation of a new Securities Market Law in 2005.

17. See Rafael La Porta, Florencio López de Silanes & Guillermo Zamarripa, *Related Lending* 13–15 (Yale Int'l Ctr. for Fin. [ICF], Working Paper No. 02–19, 2002), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=302128](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=302128) (discussing evidence of tunneling in Mexico's banking sector).

18. This refers to civil law jurisdictions with weak judiciaries, government corruption, and markets with concentrated ownership structures, in which the primary corporate governance concern is limiting self-dealing rather than reducing agency costs.



vance in the past decade. There was, no doubt, resistance by incumbent market participants opposing governance and disclosure. But there were also competing forces that countered this resistance and at times prevailed, even if it meant creatively avoiding the formal legal system and implementing corporate governance through self-regulatory regimes, as in the case of Brazil's Novo Mercado market segment.

Emerging markets' inclination to pursue a more stringent enforcement of their securities laws in the global marketplace might seem obvious today. Few would question that securities enforcement brings about investor protection and, consequently, capital market development and economic growth. Yet, these theories on the benefits of securities enforcement have only been empirically tested to a limited extent and the associations claimed are not all certain.

It is debatable which variables should be used as proxies for enforcement to explain development. Measuring enforcement in terms of regulators' powers may be a rather "law in books" approach that does not account for actual implementation. Regulators' resources might not translate into real market supervision efforts. Enforcement activity can be misleading as a variable, too. Enforcement action is, after all, a function of the underlying compliance. A jurisdiction with a low volume of securities enforcement activity may be one with a high level of compliance by market participants. Such jurisdiction might also be one in which regulation alone deters wrongdoing. More actions and sanctions do not necessarily reflect effective enforcement and/or higher regulatory intensity.

Moreover, these measures are not readily comparable across jurisdictions, given differences in the wrongdoing targeted, enforcement designs, and tool-kits, among many others. The benefits of enforcement, or lack thereof, vary across time and jurisdictions and are simply difficult to measure.<sup>19</sup>

Nevertheless, there appears to be widespread consensus among jurisdictions that corporate law and its enforcement matter. Perceptions on the importance of enforcement for their development may alone explain why Latin American markets undergoing convergence would shift toward enhanced enforcement in the global context, as well be influenced by enforcement-driven frameworks with multiple-enforcement channels and singular regulatory intensity, like the U.S. model. Enforcement may be perceived by these markets as a key piece of the financial and economic development puzzle that explains the leading position of devel-

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19. See Jackson, *supra* note 6, at 256.

oped financial systems—a piece that yields benefits such as reducing informational asymmetry and a firm’s cost of equity capital.<sup>20</sup> Such perceptions may speak to why investors are willing to pay a premium for the shares of an issuer that subjects itself to a particularly stringent regime. In the global arena, it may be considered a trigger to the “investor protection signaling” believed to attract cross-listings, decoding the *functional convergence* phenomenon behind the *bonding hypothesis*.<sup>21</sup>

On the assumption that enforcement makes a difference, and in spite of the challenges in measuring it, academic literature, economic development programs, and policy makers have continued to explore the intensity of jurisdictions’ securities laws enforcement. Recent efforts have provided preliminary empirical evidence that begins to decipher regulatory intensity on the surface, and to associate it with the size and development of markets.

Comparisons across several jurisdictions have been made, in terms of both inputs, by way of resources allocated to public enforcement (for example, staffing and budget), as well as outputs, in the form of actual enforcement activity exerted.<sup>22</sup> Preliminary findings for these jurisdictions have reported that common law countries with more developed markets incur higher enforcement costs and enforcement activity volume than their civil law counterparts.<sup>23</sup> Regulators’ resources allocated for market supervision have also been employed as enforcement proxies<sup>24</sup> and have associated public enforcement with robust markets.<sup>25</sup>

To provide an example, the literature has defined the “U.S. Model” as one that (1) pursues the enforcement of securities laws with singular in-

20. See Coffee, *The Impact of Enforcement*, *supra* note 6, at 244–46 (suggesting that the U.S.’s greater emphasis on enforcement reduces informational asymmetry and provides for a lower cost of equity capital).

21. See John C. Coffee, Jr., *The Future as History: The Prospects for Global Convergence in Corporate Governance and Its Implications*, 93 NW. U. L. REV. 641, 691–95 (1999). According to the bonding hypothesis set forth by Coffee, foreign firms opt into higher regulatory or disclosure standards, thereby committing (bonding) to more stringent governance standards than those of their domestic markets. Consequently, these firms have access to benefits such as raising equity capital and increasing shareholder value. Coffee further posits that, in seeking the mentioned benefits, firms may achieve functional convergence by simply listing on a foreign stock exchange and “renting” its higher governance standards, without having to rely on their respective local laws being reformed.

22. See Jackson & Roe, *supra* note 11, at 8.

23. See Jackson, *supra* note 6, at 256, 272.

24. See La Porta et al., *Securities Laws*, *supra* note 7, at 27–28.

25. See Jackson & Roe, *supra* note 11, at 32.

tensity,<sup>26</sup> and does so via (2) a dynamic blend of enforcement channels and enforcers. This “multiple-enforcers”<sup>27</sup> approach involves public enforcement by an “enforcement-driven” securities regulator in partnership with other equally active law enforcement agencies, coupled with an entrepreneurial private enforcement system of class and derivative litigation and a quasi-governmental self-regulatory regime in which markets are practically regulators.<sup>28</sup> Ongoing academic debate highlights the dynamics of this model by discussing whether private or public enforcement is more highly associated with robust markets (“private” vs. “public primacy” views),<sup>29</sup> and by exploring how the different enforcement modes fill each other’s gaps or serve as supplements to one another (the “multiple mechanisms” view).<sup>30</sup> Regardless of whether the private, public, or multiple-mechanisms primacy views empirically come out ahead, one may expect to find an active interplay of each enforcement mode exerting remarkable regulatory intensity.

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26. See Coffee, *The Impact of Enforcement*, *supra* note 6, at 245; Jackson, *supra* note 6, at 281; Robert Litan, *Section III: Enforcement*, in INTERIM REPORT, *supra* note 10, at 71–92.

27. See James J. Park, *Rules, Principles, and the Competition to Enforce the Securities Laws*, 100 CAL. L. REV. 115 (2012) providing a comprehensive analysis of the centralization debate revolving around the “multiple-enforcers” model characteristic of the United States’ securities enforcement system.

28. Rob Baggott, *Regulatory Reform in Britain: The Changing Face of Self-Regulation*, 67 PUB. ADMIN. 435, 437 (1989). Considering self-regulation as a matter of degree, Baggott classifies it, among other criterion, with regards to its legal status. In essence, a self-regulatory regime would be governed by mere voluntary agreements. However, statutory law often backs these agreements, and it is not uncommon for governments to reserve powers for overseeing and enforcing self-regulation.

29. Ongoing academic debates highlight the dynamics of this model by, for instance, discussing whether private and/or public enforcement prevail in better explaining capital market development. See Simeon Djankov et al., *The Law and Economics of Self-Dealing*, 88 J. POL. ECON. 430, 443–52 (2008); La Porta et al., *Securities Laws*, *supra* note 7, at 2–3; WORLD BANK, INSTITUTIONAL FOUNDATIONS FOR FINANCIAL MARKETS 5–7 (2006), *available at* <http://siteresources.worldbank.org/INTTOPACCFINSER/Resources/Institutional.pdf>. For competing views, see Jackson & Roe, *supra* note 11, at 15–16 and Armour et al., *supra* note 11, at 722.

30. See Michael Klausner, *Are Securities Class Actions “Supplemental” to SEC Enforcement? An Empirical Analysis* 6 (Feb. 23, 2010) (unpublished manuscript), *available at* [http://www.law.upenn.edu/academics/institutes/ile/PNYUPapers/2010/Klausner\\_Are%20Securities%20Class%20Actions.pdf](http://www.law.upenn.edu/academics/institutes/ile/PNYUPapers/2010/Klausner_Are%20Securities%20Class%20Actions.pdf).

It might just be that “[t]he United States has the toughest administrative enforcement of securities laws in the world.”<sup>31</sup> Annualized data from 2002–2004 suggests both the singular intensity and the “multiple-enforcers” at play—the SEC, the Department of Justice, the state regulators, and at the time, NASD and NYSE—yielding an impressive yearly average of 3,624 public actions resulting in \$5,287,483,485 in penalties. Of these, 639 actions were imposed by the SEC, amounting to \$2,164,666,667 in monetary sanctions (respectively, 17.6% and 40.9% of the total).<sup>32</sup>

Of course, the U.S. enforcement model could be considered an outlier. The high degree of regulatory intensity that it has presented in recent years may even border on “over-enforcement” (enforcement in excess of what is needed to deter and compensate), affecting capital market competitiveness and, consequently, development. The burden of excessive enforcement, namely extreme consequences for wrongdoing, may lead domestic firms to avoid raising capital through U.S. securities markets, let alone foreign issuers who simply stay away.<sup>33</sup> A healthy balance should be sought after by securities markets, and this concern has not gone unnoticed by Latin American jurisdictions.<sup>34</sup> However, if companies commonly cite U.S. enforcement as the most important reason why they avoid the U.S. market, it is arguably also one of the market’s main strengths.<sup>35</sup> Moreover, the emerging markets of Latin America have likely not reached the point of over-enforcement yet. Any increase in regulatory intensity and enforcement at their earlier stages of capital market development would be perceived as a positive sign and a shift in the direction of competitiveness and investor protection.<sup>36</sup>

Yet, it is debatable whether emerging jurisdictions undergoing convergence should adopt the features that set the securities enforcement systems of developed markets apart. Emerging jurisdictions tend to have smaller markets with concentrated ownership structures, rather than

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31. Litan, *supra* note 26, at 71.

32. See Jackson, *supra* note 6, at 256, 272. All currency references depicted with a “\$” shall refer to U.S. dollars.

33. Presumably rushed and political responses to crises during the past decade, as some have considered of both the Sarbanes-Oxley and Dodd-Frank Acts, could play into this phenomenon.

34. See Eugenio J. Cárdenas, *Mexican Corporations Entering and Leaving U.S. Markets: An Impact of the Sarbanes-Oxley Act of 2002?*, 23 CONN. J. INT’L L. 281, 296–97 (2008).

35. See Litan, *supra* note 26, at 72–81.

36. Conversation with Troy A. Paredes, Comm’r, U.S. S.E.C. (U.S. S.E.C., Washington, D.C., Oct. 2011).

deeper ones with dispersed shareholders. They normally suffer from weak judiciaries, government corruption, and low investor protection. Additionally, their primary corporate governance concern is usually limiting self-dealing, rather than focusing on reducing agency costs. They also belong to a different legal tradition,<sup>37</sup> and ongoing social change has led them to develop distinct *legal cultures*—attitudes and values with regard to law.<sup>38</sup> Hence, their needs, in terms of legal structures and institutional designs, are bound to vary accordingly. Nonetheless, many of the elements included in the enforcement “tool-kits” of developed markets could be beneficial to emerging markets and serve as an effective roadmap for them.<sup>39</sup> It is no wonder that Latin American regulators regularly request technical assistance on enforcement provided by regulators in developed markets, including the SEC and the Financial Industry Regulatory Authority (“FINRA”).

In sum, one might expect that Latin American securities markets perceive securities enforcement as beneficial to their development and, hence, are focused on shifting toward enhanced regulatory intensity via the adoption of institutional designs employed by the more developed markets to the extent that it suits them. Selected instances regarding Brazil may reveal this shift in the section that follows.

## II. A SHIFT IN THE DYNAMICS OF SECURITIES ENFORCEMENT IN BRAZIL

### *A. A New Wave in the Regulatory Evolution of Brazil's Securities Market*

A third regulatory era in the evolution of Brazil's securities markets surfaced by the turn of the century, and continued through the past decade.<sup>40</sup> Characterized by a wave of legal and institutional corporate re-

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37. Namely Civil Law, Common Law, and hybrid systems.

38. See LAWRENCE M. FRIEDMAN, *THE LEGAL SYSTEM: A SOCIAL SCIENCE PERSPECTIVE* 193–223 (1975).

39. See Z. Scott Birdwell, *The Key Elements for Developing a Securities Market to Drive Economic Growth: A Roadmap for Emerging Markets*, 39 GA. J. INT'L & COMP. L. 535, 543–44 (2011).

40. Maria Helena de Santana, CVM's Chair, identifies three stages in the regulatory evolution of Brazil's securities market. During the first stage (1964–1976) the financial system was structured. A Securities Market Law (Law 4.728 of 1965)—was enacted, and market discipline began to emerge. Lei No. 4.728, de 14 de Julho de 1965, DIÁRIO OFICIAL DA UNIÃO [D.O.U.] de 16.7.1965 (Braz.). However, the absence of a securities regulator proved to be a shortcoming. Market supervision was in the hands of the Central Bank, to which investors were not of priority. Speculation due to lack of information and disclosure, market intermediaries and issuers without accountability, and poor oversight

form, this period was also defined by important signs of capital market development. Among other indicators, trading volume and market capitalization grew substantially,<sup>41</sup> as did initial public offerings.<sup>42</sup> The number of investment funds practically doubled.<sup>43</sup> The shift toward dispersed ownership became more evident too.<sup>44</sup>

To name just a few regulatory highlights, corporate governance reform found its way into the securities market early in the emergence period, if not as a matter of legislation at first, due to resistance by the incumbent

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and enforcement, among other factors, contributed to the stock market crisis of 1971 and 1972. A second stage (1976–2001) began with reaction to the crisis, aimed at legal reform to promote accountability and duties of market intermediaries and issuers. Based on the U.S. SEC model, a new securities market law (Law 6.385 of December 7, 1976) was enacted and, with it, the Brazilian CVM came to life as an autonomous regulator with regulatory, supervisory, and sanctioning powers. *See* Lei No. 6.385, de 7 de Dezembro de 1976, D.O.U. de 09.12.1976 (Braz.). CVM's enforcement powers were, however, shared with the National Monetary Council and penalties were relatively insignificant. Brazil's Corporations Law (Law No. 6.404) was also enacted, defining a legal framework for the public firm, aimed at enhancing investor confidence and protection. *See* Lei No. 6.404, de 15 de Dezembro de 1976, D.O.U. de 17.12.1976 (Braz.). Among other features, the law provided for officer and director accountability, and for specific minority rights, enhancing disclosure, and imposing compulsory dividends. Still, the reform was not considered to have much impact in market development. Inefficient management could not be replaced through takeover activity, and firm expropriation ("tunneling") was not properly dealt with. Brazil lacked the desired capital market culture and faced economic problems, such as the inflationary environment that deterred long-term investment during the 1980s. It was not until 1997 that the Securities Market Law (Law 6.385) underwent reform, boosting enforcement of the regulator, by increasing penalties and allowing settlement agreements. *See* Lei No. 6.385, de 14 de Julho de 1965, D.O.U. de 16.7.1965, *redação dada pela* Lei No. 9.457, de 5 de Maio de 1997, D.O.U. de 6.5.97 (Braz.). However, real implementation of these enforcement mechanisms did not materialize until the turn of the century, during the third stage (2001–present) described above. For more details, see Santana, *supra* note 12.

41. Alexandre Pinheiro dos Santos, *Mitigating the Impact of Financial Crises on the Brazilian Capital Market*, in 3 *WORLD BANK LEGAL REVIEW: INTERNATIONAL FINANCIAL INSTITUTIONS AND GLOBAL LEGAL GOVERNANCE* 337 (Hassane Cissé et al. eds., 2012). Market capitalization increased from \$225 billion in 2000 to \$1.5 trillion in 2010. The daily average trading of shares increased from \$348 million to over \$3 billion.

42. Public offerings of equities totaled \$133 billion in 2010, doubling the amount of 2009. Regarding IPOs, the total amount reached \$2.1 billion in the first quarter of 2011. *Id.*

43. During the past decade—to over 10,000. *Id.*

44. *Id.* at 335, 337.

regime, through self-regulation.<sup>45</sup> Sweeping legal reform included changes to the Corporations Law No. 6.404,<sup>46</sup> providing for a series of clearly specified minority shareholder rights.<sup>47</sup> An impressive array of rules on financial disclosure was issued on an ongoing basis, particularly in the latter part of the decade.<sup>48</sup> Additionally, active coordination among financial governing bodies, focused on improving policy and regulation,<sup>49</sup> became a clear trend, as did convergence with international standards.<sup>50</sup>

Nonetheless, developments in the realm of enforcement of Brazil's securities market deserve the most attention. Early in this recent regulatory phase, important foundations in the area of market surveillance were laid down for Brazil's regulatory and institutional framework. Among others,

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45. *See id.* at 338. Via the Novo Mercado, established in 2000 as a listing segment of the, then, Sao Paulo Stock Exchange, today BM&BOVESPA S.A.-Securities, Commodities and Futures Exchange.

46. *See* Lei 10.303, de 31 de Outubro de 2001, D.O.U. de 01.11.2001 (Braz.) (altering and adding provisions to Law No. 6.404, governing corporations, and Law No. 6.385, governing the securities market).

47. Among other provisions introduced were tag-along rights; the right of preferential (non-voting) shareholders to appoint a board member, initial public offerings ("IPOs") for the case of increase in control; and the reduction of the limit of non-voting shares issued. *See id.*

48. *See* Pinheiro dos Santos, *supra* note 41, at 339–40. Examples of substantive rules issued by CVM, following the 2008 global financial crisis, may be cited. These include improving information disclosed by issuers on financial and derivative instruments (Instrução CVM No. 475, de 17 de Dezembro de 2008, D.O.U. de 22.12.2008 (Braz.)); disclosure regarding corporate governance practices, risk management controls, issuers' compensation and stock option plans (Instrução CVM No. 480, de 7 de Dezembro de 2009, D.O.U. de 11.12.2011 (Braz.)); and the regulation of public requests by management for the exercise of voting rights via proxy, including the disclosure of information to be made electronically available prior to a shareholders' meeting (Instrução CVM No. 481, de 17 de Dezembro de 2009, D.O.U. de 02.02.2010 (Braz.)).

49. Examples include the Capital Markets Working Group—established as an ongoing joint effort of the different sectors of the financial system to produce policy on capital market development. Led by the Minister of Economic Policy, it is conformed by CVM, the Central Bank, SUSEP, SPC, the Ministry of Finance and the IRS. The Committee for Regulation and Supervision of Financial markets, Capital, Insurance, and Private Pension Plans ("COREMEC"), created in 2006 and aimed at reaching bilateral agreements on financial regulation and enforcement. Conformed by the President and the Director of each of the following bodies: Central Bank, CVM, SPC and SUSEP.

50. Examples include CVM signing the IOSCO Multilateral Memorandum of Understanding for Cooperation and Assistance in 2009. *See* Int'l Org. of Sec. Commissions [IOSCO], Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information [MMoU] (May 2002), *available at* <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD126.pdf>.

the Securities Act underwent significant reform in 2001, strengthening the organization and structure of Brazil's CVM.<sup>51</sup> The agency was given exclusive oversight over securities markets, which it previously shared with the National Monetary Council, granted administrative and budgetary independence aimed at political independence, and provided with a wider scope of supervision, including oversight of investment funds, collective investment vehicles, and the derivatives, commodities, and futures markets. Serious corporate wrongdoings, including insider trading and market manipulation, were criminalized,<sup>52</sup> and tools, like the ability to settle cases, were made available to the securities regulator as well.

Nevertheless, implementation of this enforcement framework did not become prominent until the latter half of the decade. There may be multiple explanations for the sudden surge in enforcement activity, particularly given that Brazil's securities market was increasingly growing in the global context, in the midst of the global financial crisis of 2008.<sup>53</sup> The number of market participants and wrongdoing likely grew as well, a scenario in which regulatory reaction and enforcement would have made sense. However, a catalyst for the enhancement of regulatory intensity actually began in 2005: a shift in policy by Brazil's CVM, making enforcement its primary area of priority. CVM evolved into an ex-post enforcement-driven agency, somewhat resembling enforcement systems of developed markets, both in light of the adoption and implementation of new institutions and enforcement practices, and the revival of old ones. Accordingly, there was a rise in enforcement activity.

The following section identifies and discusses selected accounts that may suggest this enhanced regulatory intensity in the enforcement of Brazil's securities laws, both in terms of institutional enforcement design and its implementation.

### *B. Enhanced Regulatory Intensity in Brazil's Securities Market?*

Drawing from particular guidelines of a regulatory model to effective enforcement for emerging markets may contribute to identifying the developments of securities enforcement in Brazil during the past decade.<sup>54</sup> This regulatory system roadmap focuses mainly on the securities regulator, but also on the partnerships that it develops with the industry and

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51. See Lei 10.303, de 31 de Outubro de 2001, D.O.U. de 01.11.2001 (Braz.).

52. Including insider trading and market manipulation. See *id.*

53. See Pinheiro dos Santos, *supra* note 41, at 337–39.

54. See Birdwell, *supra* note 39, at 543–44.



other law enforcement agencies. The steps of this roadmap that I particularly select for the purposes of this study—to assess Brazil—are:

1. Political independence of the securities regulator
2. A stand-alone enforcement program with a mandate
3. The capacity to identify, target, and sanction serious securities violations (i.e. financial disclosure fraud, insider trading, market manipulation)
4. Comprehensive compulsory investigative authority (i.e. to obtain bank records, telephone and online records, witness statements)
5. A tool-kit to engage in real-time enforcement (i.e. asset freezing and financial intelligence units)
6. Recourse to an effective judiciary with specialized tribunals
7. Access of the regulator to efficient and effective civil action and remedies in the first instance
8. The ability to settle cases
9. Developing a partnership with the criminal authorities
10. Developing a partnership with the industry through a self-regulatory model
11. Developing partnerships with the international community to maximize cooperation

The analysis that follows further explains and details these guidelines, and evaluates how they have played out in light of recent developments in Brazil's securities enforcement system.

## 1. Public Enforcement

### *a. Political Independence and Boosted Resources?*

An essential aspect of this roadmap is the political independence of the regulator.

A capital market regulator should be structured by law as an independent regulatory and law enforcement agency. It should be empowered with the discretion to regulate, investigate, and bring enforcement proceedings to protect investors and to keep the capital market clean and honest, all while free of political influence.<sup>55</sup> This element is one of the principles established by the International Organization of Securities Commissions ("IOSCO").<sup>56</sup>

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55. *Id.* at 552–56.

56. IOSCO, OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION 3–4 (2010), available at <http://www.compliance-exchange.com/governance/library/ioscoprinciples2010.pdf>.

Unfortunately, Latin American securities regulators have traditionally been under the umbrella of the executive power. Finance ministries appoint and remove the heads of agencies,<sup>57</sup> and also approve of personnel hiring. The executive branches also have control over the budget, and may authorize proposed rules and exercise enforcement powers. This breadth of executive control has affected the operational and budgetary autonomy of regulators across the region for years.

During the past decade, Brazil's CVM has adopted this important cornerstone of the enforcement wish list, setting an important precedent for the region. In a significant institutional change during the wave of reform that swept Brazil in the past decade,<sup>58</sup> the Securities Act was amended in 2001,<sup>59</sup> declaring CVM an independent government agency, endowed with administrative autonomy, and free from the restraints of hierarchic subordination. In addition, it was also granted financial and budgetary autonomy.<sup>60</sup>

Moreover, the reform provided a fixed mandate for each of the five members of the Board of Commissioners. Following the SEC model,<sup>61</sup> CVM's commissioners, including the Chair, are appointed by the President of the Republic and ratified by the Senate<sup>62</sup> for five-year terms, with one new member elected each year on a staggered basis. In addition, commissioners may only be removed if they are convicted of a serious crime. This should, in theory, provide for stability and political independence of the Board of Commissioners, allowing them decision-making freedom and effective action.

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57. For example, Mexico's Minister of Finance may discretionally appoint and remove the head of the agency. Brazil appears to be leading this tendency, which other markets have followed as well, including Colombia.

58. See Fifth Meeting of the Latin American Corporate Governance Roundtable, Rio de Janeiro, Braz., Oct. 8–9, 2004, *The Legal, Regulatory and Institutional Framework for Enforcement Issues in Latin America: A Comparison of Argentina, Brazil, Chile, Colombia and Peru* 2 (2004) (by Daniel Blume), available at <http://www.oecd.org/dataoecd/32/30/34254149.pdf>.

59. Through the enactment of Law 10.411 of February 26, 2002. Lei No. 10.411, de 26 Fevereiro de 2002, D.O.U. de 27.02.2002 (Braz.).

60. See *id.* art. 1.

61. See Santana, *supra* note 12.

62. Lei No. 6.385, art. 6, de 7 de Dezembro de 1976, D.O.U. de 09.12.1976, *redação dada pela Lei No. 9.457, de 5 de Maio de 1997, D.O.U. de 6.5.97* (Braz.).

The law, however, provides that CVM is linked to Brazil's Ministry of Finance.<sup>63</sup> In principle, this link should not pose a threat to the agency's independence, but rather allow for accountability—an element that should characterize securities regulators.<sup>64</sup> In fact, Congress and the Ministry of Finance,<sup>65</sup> through its Department of Internal Control, oversee CVM's activities.<sup>66</sup>

Nevertheless, the law in action reveals particular shortcomings. For instance, CVM does not actually have the financial and budgetary autonomy that is provided for by law. The budget is centrally managed through Brazil's treasury department and an amount is allocated to the agency every year. CVM does not manage its own revenue, and the income that it generates—via fines, settlements, and an “enforcement tax”<sup>67</sup> paid by market participants, goes directly to the central government for distribution.<sup>68</sup> As a result, a significant surplus has been reported in recent years, with CVM's revenues being much in excess of the amount that it receives from the annual budget.<sup>69</sup> The agency has not received the desired budget to carry out its operations, mainly due to government focus in other priority areas.<sup>70</sup>

One illustration involves the 2009 approval of 165 new staff positions for CVM. Other government priorities have prevented CVM from hiring these allocated employees. This impingement on CVM's financial autonomy also extends to its administrative and operational independence, not only because it involves the hiring of personnel, but also be-

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63. See Lei No. 10.411, art. 1, de 26 Fevereiro de 2002, D.O.U. de 27.02.2002, amending Lei No. 6.385, art. 5, de 7 de Dezembro de 1976, D.O.U. de 09.12.1976 (Braz.).

64. See Birdwell, *supra* note 39, at 555.

65. Lei No. 6.385, art. 5, de 7 de Dezembro de 1976, D.O.U. de 09.12.1976, *redação dada pela* Lei No. 10.411, art. 1, de 26 Fevereiro de 2002, D.O.U. de 27.02.2002 (Braz.).

66. CVM undergoes several audits each year which result in a report with recommendations on its activities. Brazil's Court of Public Account also revises CVM's activities. See, e.g., CVM RELATÓRIO DE GESTÃO 2005, *supra* note 14.

67. CVM's 2005 Annual Report noted that 91% of the income came from these alternative sources. *Id.* In 2007, this tax was reported to have amounted \$60 million. CVM RELATÓRIO DE GESTÃO DO EXERCÍCIO DE 2009 [ANNUAL REPORT 2009] 29 (2009) (Braz.) [hereinafter CVM RELATÓRIO DE GESTÃO 2009], available at <http://www.cvm.gov.br/port/relgest/RelatóriodeGestãoCVM2009.pdf>. According to 2009 report the amount of fines totaled \$29 million in 2007, but totaled \$65.5 million in 2006. *Id.*

68. CVM RELATÓRIO DE GESTÃO 2009, *supra* note 67, at 15.

69. *Id.*

70. Telephone Interview with Maria Helena dos Santos Fernandes de Santana, Chair of CVM & IOSCO's Exec. Comm. (Oct. 10, 2011) [hereinafter Santana Interview].

cause a significant number of these new employees were to be allocated to enforcement and surveillance efforts.<sup>71</sup>

However, since 2005, after CVM's management decision to prioritize enforcement, the central government has strived to provide the agency with increased resources.<sup>72</sup> Data reported by the Latin American Corporate Governance Roundtable reveals that CVM's budget, which amounted to \$25.8 Million in 2004, increased to \$77.2 million in 2007 and \$90.67 million in 2008, a significant rise of 84.6% (in terms of adjusted local currency).<sup>73</sup> However, as shown in the following table, the increase during the mentioned time period is not nearly as impressive after normalizing the budget in relation to the size of the market, in terms of market capitalization.

Moreover, to what extent these resources were actually allocated to enforcement is difficult to determine, but a breakdown of CVM's budget provides a fairly accurate snapshot.<sup>74</sup> A significant percentage of CVM's budget was allocated to an account described as Capital Market Development, which at least indirectly is aimed at investor protection. However, it appears that only a relatively small percentage of that account

71. *Id.*

72. *Id.*

73. See Tenth Meeting of the Latin American Corporate Governance Roundtable, Santiago, Chile, Dec. 1–2, 2008, *The Legal, Regulatory and Institutional Framework for Enforcement Issues in Latin America: A Comparison of Argentina, Brazil, Chile, Colombia, Panama and Peru* 3 (2009) (by Andreas Grimminger et al.) [hereinafter *2009 Framework for Enforcement Issues*], available at <http://www.oecd.org/dataoecd/0/15/44138533.pdf>.

74. Annual National Budgets of Brazil 2004–11. See Lei No. 10.837, de 16 de Janeiro de 2004, Orçamento Anual de 2004 [Annual Budget], Janeiro 2004 (Braz.), available at <http://sidornet.planejamento.gov.br/docs/lei2004/index.htm>; Lei No. 11.100, de 25 de Janeiro de 2005, Orçamento Anual de 2005 [Annual Budget], Janeiro 2005 (Braz.), available at <http://sidornet.planejamento.gov.br/docs/lei2005/index.htm>; Lei No. 11.306, de 16 de Maio de 2006, Orçamento Anual de 2006 [Annual Budget], Maio 2006 (Braz.), available at <http://sidornet.planejamento.gov.br/docs/lei2006/>; Lei No. 11.451, de 07 de Fevereiro de 2007, Orçamento Anual de 2007 [Annual Budget], Fevereiro 2007 (Braz.), available at [http://www.planejamento.gov.br/secretarias/upload/Legislacao/Leis/070207\\_lei\\_11451.pdf](http://www.planejamento.gov.br/secretarias/upload/Legislacao/Leis/070207_lei_11451.pdf); Lei No. 11.647, de 24 de Março de 2008, Orçamento Anual de 2008 [Annual Budget], Março 2008 (Braz.), available at [http://www.planejamento.gov.br/secretarias/upload/Legislacao/Leis/080324\\_lei\\_11647.pdf](http://www.planejamento.gov.br/secretarias/upload/Legislacao/Leis/080324_lei_11647.pdf); Lei No. 11.897, de 30 de Dezembro de 2008, Orçamento Anual de 2009 [Annual Budget], Dezembro 2008 (Braz.), available at [http://www.planejamento.gov.br/secretarias/upload/Arquivos/sof/orcamento\\_09/loa09/Loa\\_2009.pdf](http://www.planejamento.gov.br/secretarias/upload/Arquivos/sof/orcamento_09/loa09/Loa_2009.pdf); Lei No. 12.214, de 26 de Janeiro de 2010, D.O.U. de 27.01.2010 (Braz.); Lei No. 12.381, de 9 de Fevereiro de 2011, D.O.U. de 10.02.2011 (Braz.).

(4.9% annualized average) was actually designated for Market Supervision, Regulation, and Investor Protection.

<b>CVM Budget 2004–2011</b> <sup>75</sup>								
("S" Indicates Brazilian Currency in Millions, Decimals Reflect Percentages)								
	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
I. Total Financial System Budget (Nominal Value)	\$8,614	\$10,146	\$10,340	\$13,119	\$14,342	\$19,862	\$19,219	\$19,702
Real Value (Adj. to inflation)	\$12,221	\$13,620	\$13,458	\$16,346	\$16,874	\$22,403	\$20,468	\$19,702
Normalized to Market Capitalization	0.98158	0.91825	0.68269	0.54152	1.03462	0.85642	0.74639	0.86051
A. Total CVM Budget (Nominal Value)	\$75.40	\$79.40	\$94.00	\$140.20	\$162.90	\$201.90	\$191.20	\$267.40
Real Value (Adj. to inflation)	\$106.98	\$106.59	\$122.35	\$174.69	\$191.66	\$227.73	\$203.63	\$267.40
Normalized to Market Capitalization	0.00859	0.00719	0.00621	0.00579	0.01175	0.00871	0.00743	0.01168
% of Financial System Budget	0.88	0.78	0.91	1.10	1.40	1.00	1.00	1.40
I. Capital Market Development	\$59	\$66.40	\$77.50	\$98.10	\$99.60	\$101	\$124.30	\$134.60
Real Value (Adj. to inflation)	\$84	\$89.14	\$100.87	\$122.23	\$117.18	\$114	\$132.38	\$134.60
Normalized to Market Capitalization	0.00672	0.00601	0.00512	0.00405	0.00719	0.00435	0.00483	0.00588
% of CVM's Budget	78.00	83.60	82.50	70.00	61.00	50.00	65.00	50.30
a. Market Supervision, Regulation & Investor Protection	\$4.11	\$3.22	\$2.99	\$7.73	\$9.53	\$3.61	\$6.60	\$6.90
Real Value (Adj. to inflation)	\$2.48	\$2.74	\$4.76	\$9.04	\$8.92	\$4.83	\$6.82	\$6.90

75. Author's compilation. Budget collected from Brazil's Annual National Budgets 2004–2011 (see *supra* note 74), was adjusted for inflation (real value in terms of 2011 BRCy) based on Brazil's Consumer Price Index ("CPI")—Calculated from annualized data on inflation obtained at: INFLATION, <http://www.inflation.eu> (last visited May 29, 2012), and normalized in relation to Market Capitalization of BM&FBOVESPA stock

Normalized to Market Capitalization	0.00033	0.00022	0.00015	0.00026	0.00058	0.00014	0.00024	0.00030
% of Capital Market Development	4.90	3.60	3.00	6.30	8.00	3.20	5	5
<i>i. Investor Protection &amp; Assistance</i>	\$1.10	\$0.81	\$0.71	\$1.30	\$1.40	\$1	\$1.40	\$1.40
Real Value (Adj. to inflation)	\$1.56	\$1.09	\$0.92	\$1.62	\$1.65	\$1	\$1.49	\$1.40
Normalized to Market Capitalization	0.00013	0.00007	0.00005	0.00005	0.00010	0.00004	0.00005	0.00006
<i>ii. Market Supervision</i>	\$0.80	\$0.80	\$0.80	\$2.50	\$3.30	\$9.30	\$1.20	\$2.00
Real Value (Adj. to inflation)	\$1.14	\$1.07	\$1.04	\$3.11	\$3.88	\$10.49	\$1.28	\$2.00
Normalized to Market Capitalization	0.00009	0.00007	0.00005	0.00010	0.00024	0.00040	0.00005	0.00009
<i>iii. Information Dissemination &amp; Regulation</i>	\$1.10	\$0.81	\$0.80	\$2.40	\$3.40	\$1.30	\$3.50	\$3.50
Real Value (Adj. to inflation)	\$1.56	\$1.09	\$1.04	\$2.99	\$4.00	\$1.47	\$3.73	\$3.50
Normalized to Market Capitalization	0.00013	0.00007	0.00005	0.00010	0.00025	0.00006	0.00014	0.00015

With regards to staff, the Commission also showed an upward trend during the decade. The number of employees increased from 363 in 2004 to 500 in 2008.

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exchange—end of year market capitalization data from 2004–2011 obtained at: WORLD FEDERATION OF EXCHANGES, <http://www.world-exchanges.org/> (last visited June 7, 2012). The market capitalization data was converted from U.S. Dollars to Brazilian Currency using the end of the year exchange rate (Dec. 31) obtained at: *Historical Exchange Rates*, OANDA, <http://www.oanda.com/currency/historical-rates/> (last visited May 29, 2012).

<b>CVM Staff 2001–2007<sup>76</sup></b>	
<b>2001</b> (January)	327 employees
<b>2003</b> (Aug.)	371 employees
<b>2004*</b>	363 employees
<b>2005</b> (Sep)	500 employees
<b>2006</b> (Aug)	487 (451 staff / 36 Federal Attorneys)
<b>2007</b>	489 (459 Staff / 30 Federal Attorneys)
<b>2008*</b>	500 employees

A significant increase occurred in 2005, reflecting CVM's strategic decision that year to prioritize on enforcement.<sup>77</sup> CVM has since continued its efforts to increase staff. As mentioned above, new employee positions were approved in 2009, but to date are on hiatus given budgetary constraints.

Moreover, as a result of CVM establishing a centralized enforcement division in 2008, it also began hiring more specialized staff to conduct investigations and pursue cases. In 2009, the department had a staff of thirty, composed of twenty-two inspectors, and eight federal prosecutors.<sup>78</sup> In addition, the Inspections Department, responsible for external inspections, had a staff of forty-two. CVM's new enforcement division is detailed in the section that follows.

*b. A Beefed-Up Enforcement Program and Increased Action*

In the roadmap to effective enforcement, a fundamental step involves the regulator establishing a "stand-alone enforcement program with a mandate."<sup>79</sup> Among other features, the program should have an enforcement division vested with the responsibility and statutory capacity to investigate and prosecute serious corporate wrongdoing. It should be able to compel evidence and prosecute, employing tools such as stopping ongoing fraud via injunctive orders and asset freezes, and to bring enforcement actions with demonstrable consequences. The program should have both investigative and prosecutorial functions, and its investigative staff

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76. *2009 Framework for Enforcement Issues*, *supra* note 73, at 7–8; ROBERT PRINGLE, HOW COUNTRIES SUPERVISE THEIR BANKS, INSURERS AND SECURITIES MARKETS 2010 (Risk Books 2009).

77. Santana Interview, *supra* note 70.

78. See *2009 Framework for Enforcement Issues*, *supra* note 73, at 3.

79. See Birdwell, *supra* note 39, at 552.

should include not only lawyers, but also accountants and personnel with experience in prosecuting cases.<sup>80</sup>

As is the case with most Latin American jurisdictions, Brazil's securities regulator did not have an enforcement department prior to 2008. Each of CVM's eleven divisions, or *Superintendencias*,<sup>81</sup> supervised, investigated, and proposed penalties regarding their areas of expertise for the Board of Commissioners to decide on. That system has advantages and continues to be implemented to this date, particularly given the in-depth technical expertise of each division. However, with its shift in policy to prioritize enforcement, CVM established a centralized enforcement program in 2008 aimed at unifying and accelerating enforcement activity.<sup>82</sup> Enforcement is jointly carried out by two divisions: the *Superintendencia de Processos Sancionadores* ("SPS") and the *Procuradoria Federal Especializada* ("PFE").<sup>83</sup>

This enforcement program's institutional design entails a unique model of administrative enforcement. Investigations are carried out by the managers and staff of SPS and PFE in collaboration with specialized federal attorneys and investigators assigned to CVM. This design reportedly resulted in increased and more focused enforcement activity, targeting serious and sophisticated wrongdoing.<sup>84</sup> Moreover, the length of even the most complex procedures has been reduced to an average of ten months.<sup>85</sup>

Carrying on with the roadmap, the ability to settle administrative matters is also an essential feature of an enforcement program and a useful part of its tool-kit.<sup>86</sup> Unique among the regulators of the region, CVM has had this power since 1997, inspired by the SEC settlement.<sup>87</sup> Known as *Termos de Compromiso*, these settlements halt an administrative proceeding if the accused party agrees to end the unlawful conduct and to correct the wrongdoing, in addition to indemnifying the corresponding loss.

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80. *Id.* at 553–54.

81. With the same hierarchical level, and headed by a Directors or *Superintendentes*. See Pinheiro dos Santos, *supra* note 41, at 343–44.

82. See *2009 Framework for Enforcement Issues*, *supra* note 73, at 4.

83. See *id.*

84. Telephone Interview with Alexandre Pinheiro dos Santos, CVM Att'y Gen. (Gen. Counsel) & Head of CVM Legal Dept. (Procuradoria Federal Especializada) (Oct. 13, 2011) [hereinafter Pinheiro Interview].

85. Pinheiro dos Santos, *supra* note 41, at 343.

86. See Birdwell, *supra* note 39, at 575–76.

87. Pinheiro dos Santos, *supra* note 41, at 343.



However, these settlements had seldom been used until the second half of the decade. Aimed at deploying this potentially useful tool, CVM established the *Committee for Settlements of Proceedings* in 2005. This committee is led by CVM's Chief Executive Officer and includes the Superintendents of each of CVM's eleven divisions. Its role broadly involves identifying and negotiating potential settlements of administrative cases and delivering opinions on proposals for settlement made by defendants or people under investigation. Proposed settlements are subject to review and approval by CVM's Board of Commissioners.

The committee has played an active role in institutionalizing the negotiations and settlement process, providing for its legitimacy. Market participants involved get to actively engage in the negotiations, which has resulted in a more open and transparent process. CVM's Board of Commissioners usually, though not always, accepts the terms proposed, which also speaks to the authority of the process.<sup>88</sup> Moreover, the reduction in the length of administrative procedures and investigations may also explain why market participants prefer to reach a settlement, rather than wait for a decision by CVM's Board of Commissioners. Further, the Enforcement Division has been bringing more cases, resulting in increased settlements.<sup>89</sup> Another aspect that may be appealing to both regulators and market participants is that these settlements are not subject to approval by the courts.

Preliminary data may speak to the increase in enforcement activity by CVM, regarding administrative action pursued via its new centralized enforcement division and settlements. Surveys conducted by the Latin American Roundtable for Corporate Governance both before and after CVM's shift in policy prioritizing enforcement reflect the contrast in enforcement between the first and second half of the decade.<sup>90</sup>

There is an upward trend in the number of administrative sanctions imposed by Brazil's securities regulator, resulting from administrative procedures. These amounted to 542 between the period from 2006 to July 2009, of which 448 were fines and 94 were suspensions.<sup>91</sup> This was an increase from the 319 sanctions imposed during the 2001–2003 period, which featured 313 fines and 6 suspensions.<sup>92</sup> Even more striking is the difference in the amount of fines imposed during the 2006–2009 period, which totaled \$279.5 million, versus a much lower \$81.7 million

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88. Santana Interview, *supra* note 70.

89. *Id.*

90. See 2009 Framework for Enforcement Issues, *supra* note 73, at 3–5.

91. *Id.* at 8.

92. *Id.*

for the 2001–2003 period.<sup>93</sup> During the recent period, the highest individual fine was also significantly higher, amounting to \$38.5 million, compared to \$22.5 million in the earlier period.<sup>94</sup>

<b>CVM Administrative Sanctions 2001–2003 / 2006–2009<sup>95</sup></b>			
	<b>Number of Fines</b>	<b>Amount of Total Fines (U.S. millions)</b>	<b>Highest Fine in period (U.S. millions)</b>
<b>2001</b>	131	–	\$22.5
<b>2002</b>	55	–	
<b>2003</b>	127	–	
<i>Total</i>	<b>313</b>	<b>\$81.7</b>	
<hr/>			
<b>2006</b>	184	\$65.5	\$38.5
<b>2007</b>	105	\$29	
<b>2008</b>	103	\$185	
<b>Jul. 2009</b>	56	–	
<i>Total</i>	<b>448</b>	<b>\$279.5</b>	

Administrative sanctions are not always final, however.<sup>96</sup> Of the 448 fines imposed between 2006 and July 2009, a very high number, 313 (over 70%) were subject to appeals processes.<sup>97</sup>

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93. *Id.* at 7.

94. *Id.*

95. *Id.* at 7–8.

96. Final decisions of CVM relating to enforcement may be appealed before the *Conselho de Recursos do Sistema Financeiro Nacional—CRSFN*, an administrative body composed of representatives of CVM, the Central Bank of Brazil, the Finance Ministry, and regulated agents. There is no possibility of appeal before the judiciary. *See id.* at 8.

97. *Id.* at 6–8.

<b>CVM Administrative Sanctions 2006–2009<sup>98</sup></b>			
	<b>Number of Fines</b>	<b>Number of Fines Appealed</b>	<b>Appeals Status In 2004 (for the 2003–2006 fines) / In 2009 (for the 2006–2009 fines)</b>
<b>2001</b>	131	114	74 upheld / 13 reversed
<b>2002</b>	55	66	14 upheld / 7 reversed
<b>2003</b>	127	87	0 upheld / 0 reversed
<i>Total</i>	<b>313</b>	<b>267</b>	<b>90 upheld / 20 reversed / 108 modified / 49 pending</b>
<b>2006–2009</b>			
<b>2006</b>	184	134	4 upheld / 10 dismissed / 120 pending
<b>2007</b>	105	81	4 upheld / 77 pending
<b>2008</b>	103	84	1 upheld / 83 pending
<b>2009 (1<sup>st</sup> semester)</b>	56	19	0 upheld / 0 dismissed / 19 pending
<i>Total</i>	<b>448</b>	<b>318</b>	<b>19 processed / 280 pending</b>

For the 2001–2003 period, most of the appeals were processed by the end of the three-year period, that is, 218 of the total 267 appeals.<sup>99</sup> Though a considerable number were upheld, and there were only a few reversals, 108 cases were modified.<sup>100</sup> What is of more concern is that for the 2006–2009 period, of the 313 appeals only 19 (6%) were actually processed by the end of that period.<sup>101</sup>

Since 2005, there has been increased focus on more sophisticated wrongdoing, particularly insider trading. Although relatively few administrative cases have been decided regarding this misconduct, they concern a considerable number of defendants. These figures reflect that enforcement activity is now visible in this area, and speak to CVM's efforts to bring action in this front.<sup>102</sup>

98. *Id.* at 7–8.

99. *Id.*

100. *Id.*

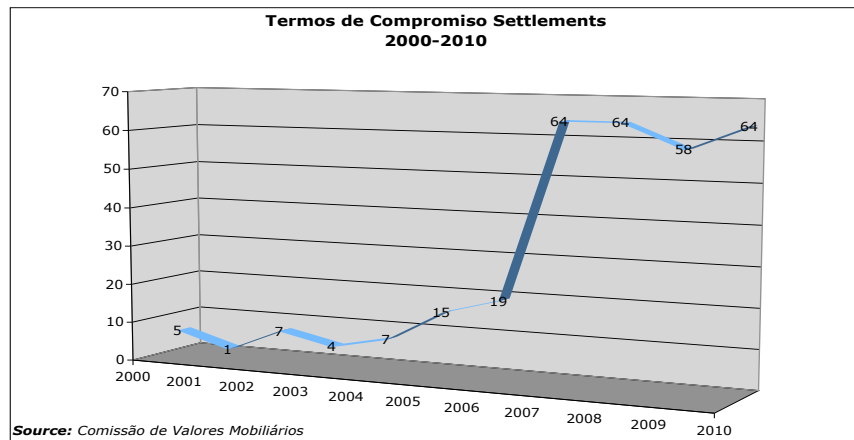
101. *Id.*

102. Pinheiro Interview, *supra* note 84.

Insider Trading Cases Judged by CVM			
Year	Number of administrative cases judged and/or with <i>Termo de Compromisso</i>	Number of defendants	Charged as Guilty or Closed with celebration of <i>Termo de Compromisso</i>
2005	4	14	2
2006	5	21	17
2007	4	40	22
2008	7	36	19
2009	3	4	2
2010	10	33	29
2011	2	3	3
<b>Total</b>	<b>35</b>	<b>151</b>	<b>94</b>

*Source: Comissão de Valores Mobiliários*

The *Termos de Compromisso* settlements have witnessed a significant increase too, as shown in the following graph. Not surprisingly, this rise began after 2005, following the establishment of the Committee for the Settlement of Procedures.



The number of settlements skyrocketed from nineteen in 2006 to over sixty in the years that followed. As shown in the table below, the number of defendants entering into the agreements surged as well, as did the total amount paid as a result. Significant amounts were paid per settlement too, with the lowest settlement signed in 2008 amounting to almost \$10,000, the average to \$53,026, and the highest to over \$3 million. In contrast, the average fine that year amounted to almost \$1.5 million, and

the highest imposed was \$38.5 million.<sup>103</sup> This considerable difference may explain not only why most administrative decisions (which impose fines) are appealed, but also why market participants increasingly consider settling.

<b>TERMOS DE COMPROMISO</b>			
<b>Year</b>	<b>Number</b>	<b>Number of defendants</b>	<b>Amount Paid (R\$)</b>
1998	2	4	\$2,679.87
1999	3	5	\$0.00
2000	5	30	\$3,347,001.77
2001	1	3	\$266,414.48
2002	7	31	\$520,000.00
2003	4	7	\$10,000.00
2004	7	23	\$254,407.97
2005	15	51	\$17,529,100.00
2006	19	96	\$1,911,986.28
2007	64	159	\$46,054,291.88
2008	64	112	\$10,660,927.80
2009	58	84	\$11,045,731.74
2010	64	141	\$57,502,975.77
2011	36	70	\$170,469,222.67
Total	349	816	\$319,574,740.23

*Source: CVM's Procuradoria Federal Especializada (PFE)*

Yet another step toward effective enforcement entails developing a partnership with the criminal justice authorities. To that end, during the latter half of the past decade, CVM actively cooperated with the Brazilian Federal Police Department and the Federal Prosecutor's Office. This joint action was the result of an inter-institutional relationship that has deepened over the past six years, which has already led to the signing of cooperation agreements among the three institutions.<sup>104</sup> This collaboration has resulted in the use of more sophisticated tools that have allowed CVM to engage in real-time enforcement. This has included the freezing of assets on a considerable number of occasions during recent years.

As previously mentioned, a series of offenses were criminalized early in the decade, including insider trading and market manipulation. Though that was an important achievement, it was not until these col-

103. See 2009 Framework for Enforcement Issues, *supra* note 73, at 7.

104. Pinheiro Interview, *supra* note 84.

laborations began that real implementation has materialized. For instance, in 2011, CVM and the Federal Prosecutors Office were able to obtain the first criminal conviction in Brazil for insider trading, in the *Sadia* case.<sup>105</sup> This active interplay among enforcers might be a reflection of Brazil moving toward a “multiple-enforcers” model.

CVM and the Federal Prosecutors office have also joined together to revive the Collective Civil Action. Though it dates back to 1989, it had not been employed until very recently, as a result of CVM’s recent enforcement efforts. Unlike U.S. class actions, the remedy is not available for market participants to file directly, but CVM and the Federal Prosecutors Office may do it on their behalf. CVM has increasingly been filing these actions on behalf of numerous market participants. The compensation obtained is then sent back to a fund to pay people who incurred losses. This process is an important instrument that is gaining relevance and momentum, though CVM is very selective in its use. Although there are not many cases to date, CVM set important precedents in recent years, particularly regarding insider trading.<sup>106</sup> One deterrent to wider use of this instrument, however, is the judiciary’s lack of expertise in capital markets matters.

Finally, in terms of maximizing its capacity to engage in international cooperation, CVM’s policy on enforcement has led it to reach out to the global community in order to improve its enforcement practices and exchange information with securities regulators around the world. Securities enforcement in Brazil follows the IOSCO Objectives and Principles of Securities Regulation. This commitment is reflected in CVM’s signing the IOSCO Multilateral Memorandum of Understanding for Cooperation and Assistance in 2009, aimed at international cooperation among regulators for pursuing the increasing amount of securities violations having international dimensions.<sup>107</sup> A more recent example of this international interplay among regulators was a technical assistance workshop on enforcement practices hosted and sponsored by CVM in May 2011, to

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105. Two former officers of Sadia, S.A. were convicted by a court and sentenced to prison and a fine. J.F.S.P., Crim. No. 2009.61.81.005123-4, 16.02.2011, 182 Diário do Judiciário Eletrônico [D.J.e.], 02.10.2009, 234 (Braz.) (on file with the author).

106. Pinheiro Interview, *supra* note 84.

107. MMoU, *supra* note 50. The fact that CVM’s chair is also the current Chair of IOSCO’s Executive Committee further reflects Brazil’s commitment with the international community regarding collaboration among regulators in terms of global market surveillance.

which the Office of International Affairs of the SEC substantially contributed through its Technical Assistance Program.<sup>108</sup>

## 2. Self-Regulation—Toward a Multiple-Enforcers Model?

A securities authority needs to develop a partnership with the industry via a self-regulatory regime.<sup>109</sup> Brazil has strong foundations in self-regulation dating back to before the turn of the century. The Brazilian Corporate Governance Institute (“IBGC”) was established in 1995 to guide qualifying directors and senior officers of companies in the application of corporate governance principles. In 1998, the National Investment Bank Association (“ANBID”) launched its self-regulatory code for public offerings of securities, imposing stricter standards than those of the legislation of the time. In 2000, the stock exchange launched the Novo Mercado and Corporate Governance Levels II and III listing segments, involving corporate government standards and requirements that also went further than the law.

CVM has supported and capitalized on these self-regulatory developments, ultimately designing an SRO regime that is both mandatory and voluntary. The mandatory dimension is of a statutory nature and involves, as legal conditions to operate, requirements to issuers. An important step came in 2007, when the Sao Paulo Stock Exchange (“BOVESPA”)<sup>110</sup> and the Brazilian Mercantile & Futures Exchange (“BM&F”)<sup>111</sup> demutualized, launched their IPOs, and merged, resulting in BM&FBOVESPA.<sup>112</sup> Practically in tandem, and foreseeing potential conflicts of interest, CVM issued Instruction No. 461/07,<sup>113</sup> providing for a detailed legal framework of self-regulation for stock exchanges and other organized markets.<sup>114</sup>

Under this framework, organized securities markets must be structured, maintained, and inspected by “managing entities” authorized by CVM,

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108. CVM & BM&FBOVESPA, *Bilateral Enforcement Program with Brazilian Regulators and Prosecutors* (May 2–6, 2011), *available at* [http://www.sec.gov/about/offices/oia/oia\\_emergtech.shtml](http://www.sec.gov/about/offices/oia/oia_emergtech.shtml).

109. *See Birdwell, supra* note 39, at 579.

110. The company that actually launched the IPO was BOVESPA Holding Group, of which the Sao Paulo Stock Exchange was a subsidiary. This took place on October 26, 2007.

111. BM&F’s IPO took place on November 30, 2007.

112. Brazil’s only stock exchange, and the third largest in the world.

113. Instrução CVM No. 461, de 23 de Outubro de 2007, D.O.U. de 24.10.2007 (Braz.) [hereinafter CVM Instruction No. 461].

114. Including OTC and commodities and futures markets.

organized as associations or stock corporations.<sup>115</sup> These managing entities are responsible for the preservation and self-regulation of the securities markets they manage, and it is their legal duty to maintain the balance between their own interests and the public interests to be served.<sup>116</sup> In turn, to perform the self-regulatory supervision and enforcement, managing entities may either (1) form an association, controlled entity, or entity under common control, or (2) outsource the task to an independent third-party.

BM&FBOVESPA is the managing entity responsible for Brazil's securities markets. Unlike the U.S. exchanges, BM&FBOVESPA has not yet outsourced its market surveillance and oversight activities to a third-party enforcer like FINRA. However, it did establish a functionally autonomous and financially independent non-profit subsidiary with considerable rule-making and enforcement powers to perform the task: BM&FBOVESPA Supervisão de Mercados ("BSM").<sup>117</sup>

A specific example of the interplay of public enforcement with self-regulation is provided by Instruction 461/07,<sup>118</sup> which establishes that in relation to penalties for violations of rules under its jurisdiction, CVM may deduct penalties that have already been imposed under mandatory self-regulation, including penalties imposed by BSM. In that respect, CVM is reported to be reasonable, and it capitalizes on this division of labor, which has reportedly proved successful in recent years and contributes to CVM's prioritizing of its resources.<sup>119</sup>

The other self-regulatory dimension is of a non-statutory nature, which CVM has promoted via regulatory incentives. These have included fast-track securities (debenture) offerings (avoiding paperwork and costs) after complying with best corporate practices, such as those established by the Investment Bank Association ("ANBID") Code regarding public offerings. Another example is CVM Instruction 471 of 2008, which offers a fast track for offerings that have been reviewed by a self-regulatory entity under an agreement with CVM.<sup>120</sup> In addition to enhancing investor confidence through disclosure practices, this has allowed CVM to save and focus its resources on other priorities.

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115. CVM Instruction No. 461/07, art. 9.

116. *Id.* art. 14.

117. BSM started operating on October 1, 2007.

118. CVM Instruction No. 461, art. 49, para. 5.

119. Santana Interview, *supra* note 70.

120. Instrução CVM No. 471, de 8 de Augusto de 2008, D.O.U. de 11.08.2008 (Braz.) [hereinafter CVM Instruction No. 471].



As a result of these developments, Brazil's securities market may be further shifting toward a "multiple-enforcers" model.

### 3. Private Rights of Action—Are They on the Way?

So far Brazil's securities enforcement system appears to satisfy several of the guidelines considered to contribute to effective enforcement. However, there is one important instrument that it does not yet offer: recourse to an effective judiciary with specialized tribunals that have the capacity to entertain capital markets matters.<sup>121</sup>

Private enforcement of securities markets violations is rare in Latin America, and Brazil is not an exception.<sup>122</sup> Market participants may resort to the Brazilian court system, but seldom do in practice. In part, this may be due to the lack of specialized judges trained in capital markets and securities regulation.<sup>123</sup> The courts also present other problems, such as lengthy procedures that become expensive. In turn, most of the cases related to corporate and securities law often result in settlement agreements, so there is even less incentive to use the courts.<sup>124</sup>

Another potential explanation involves the perception by the market that CVM is quite efficient and able to deal with very complex legal issues. This further preempts the judiciary from being activated.<sup>125</sup> If, in fact, CVM is bringing more actions, this may trigger the involvement of the courts in the foreseeable future. This scenario might provide incentives to challenge or delay a ruling by CVM, and may ultimately result in further specialization of the judiciary to handle these matters.<sup>126</sup>

Another factor worth noting is that a good number of issuers are listed in Level II of the Novo Mercado market, and accordingly are obliged to adhere to an arbitration procedure rather than resort to the courts. Unfortunately, illustrating a shortcoming of self-regulation, arbitration has not

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121. Birdwell, *supra* note 39, at 576–77.

122. See Nelson Eizirik, Concept Paper Presented at the Harvard Law School First Annual Symposium on Building the Financial System of the 21st Century: An Agenda for Latin America and the United States: Insider Trading Law in Brazil: Recent Developments 83, 83–89 (June 13–15, 2008), available at <http://www.law.harvard.edu/programs/about/pifs/symposia/brazil/2008-latam/08lafinalreport.pdf>.

123. Santana Interview, *supra* note 70.

124. *Id.*

125. *Id.*

126. *Id.*

been used by market participants, as it is often considered too expensive.<sup>127</sup>

A related step in the roadmap involves the access of a regulator to civil remedies in order to instigate action in the first instance.<sup>128</sup> Regulators in Brazil have access to civil action. However, civil remedies, as with private rights of action, are often not pursued in practice and CVM prefers to proceed administratively. Moreover, as opposed to market participants, CVM does not have the option of resorting to the state courts, which have more experience in dealing with private commercial matters than the federal courts.

The upside is that there are signs of improvement that may lead Brazil to include private rights of action in its emerging multiple-enforcers model. Judges have reportedly been receptive to this in recent matters. In what might be the most relevant collective civil action to date, CVM reportedly did not face major difficulties in presenting the matter thoroughly to the court.<sup>129</sup> Other efforts have involved collaboration agreements between CVM and the judiciary to increase communication and exchange of information concerning Brazil's capital market. During the last two to three years, CVM has designed programs for judges to participate in, yielding positive results.<sup>130</sup> CVM has also increased its interactions with the courts via amicus briefs and expert opinions regarding conflicts among market participants.

Finally, there has been a tendency toward specialization. One innovation is a specialized commercial court in Rio de Janeiro. This is still a preliminary experience that lacks institutionalization. Among other issues, problems arise when a judge is promoted and needs to be replaced. A system to keep the judges educated and specialized in the field of capital markets is needed.<sup>131</sup> More resources should also be directed toward Brazil's judiciary to establish "commercial courts . . . in the cities with stronger business activities," and to invest in specialized training.<sup>132</sup>

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127. *Id.*

128. Birdwell, *supra* note 39, at 568. Considering that it may be easier to pursue serious wrongdoing via the civil procedure, as it usually provides simpler standards of proof than the criminal path.

129. Pinheiro Interview, *supra* note 84.

130. *Id.*

131. Santana Interview, *supra* note 70.

132. See Isabella Saboya, Partner, Investidor Professional, Address at the Fifth Meeting of the Latin Am. Corp. Governance Roundtable: Legal, Regulatory and Institutional Framework for Enforcement—State of Play and Key Challenges (Oct. 8, 2004), *available at* <http://www.oecd.org/dataoecd/48/42/33940873.pdf>.

## CONCLUDING REMARKS

These preliminary findings indicate that, within the global context and during a period of ongoing legal and institutional corporate reform dating back to the turn of the century, Brazil has shifted toward enhanced regulatory intensity in the enforcement of its securities laws. The research identifies a series of developments in institutional design and implementation that reflect this shift.

This transformation in Brazil's securities enforcement system followed a 2005 change in policy whereby CVM made enforcement its main priority. Consequently, CVM became an enforcement-driven agency, embodying characteristics reminiscent of regulators in developed securities markets like the United States. This transformation involved both the development and implementation of new enforcement institutions and practices, and the resurgence of older ones that had been in place but had seldom been engaged.

Key developments suggesting enhanced regulatory intensity included the establishment of a new stand-alone enforcement program within CVM that includes a centralized enforcement program aimed at enhancing enforcement activity via two specialized divisions: the *Superintendencia de Processos Sancionadores* and the *Procuradoria Federal Especializada*. This enforcement mandate was created with a unique design, combining federal attorneys and staff with prosecutorial and investigative functions. A surge in enforcement activity, particularly regarding administrative action, penalties, and settlements, became clear after this enforcement program came into play in the second half of the decade. Other signs of improvement included swifter administrative procedures and a focus on more serious misconduct, namely insider trading and market manipulation.

In addition to administrative action, the enforcement team diversified toward both civil and criminal actions. This resulted in the revival of the Collective Civil Action, a class-action type remedy that had not been employed before, which led to an increased use of the courts. Further, a collaboration with the criminal justice authorities allowed for the successful prosecution of wrongdoing that had been criminalized earlier in the decade, and triggered the use of a more sophisticated tool-kit, including the freezing of assets and injunctive orders.

Moreover, to spark the use of an important tool that had lacked legitimacy and use—the power to settle cases—CVM created the Committee for Settlements of Proceedings. This new institution legitimized a negotiations process that resulted in a striking rise in *Termos de Compromisso* settlements, yet another sign of enhanced enforcement activity.

CVM further developed a strong partnership with the industry, establishing a self-regulatory regime with both mandatory and voluntary dimensions. On the mandatory (statutory) side, a detailed legal framework of self-regulation for organized markets was set in place, including both enhanced listing requirements for public firms and the effective outsourcing of market surveillance to a quasi-regulator SRO with enhanced rule-making and enforcement powers. On the voluntary front, significant incentives led firms to adopt higher corporate governance standards that went beyond the law.

Additional trends included international cooperation and assistance with other securities regulators of the world, the adoption of international principles involving enhanced enforcement practices, and reaching out to developed markets for technical support in order to improve market surveillance.

A surge in the resources of the securities regulator during this period, both in budget and staffing, also suggests increased focus on enforcement. However, challenges in this area became apparent, revealing limited administrative and budgetary autonomy of the regulator, restricting its access to the resources and personnel needed for market surveillance and enforcement.

Another shortcoming is the lack of specialized tribunals and judges trained in capital market matters. This may explain why private rights of action are practically null, and why procedures are sluggish and costly. It may also explain why CVM does not instigate civil action in the first instance but, rather, proceeds administratively. There are, however, tendencies that might make way for increased involvement of the courts, including attempts to establish specialized commercial courts, and recent collaboration and exchanges of information between the securities regulator and the courts.

To what extent do all these developments speak to globalization of securities enforcement and the influence of developed markets in the evolution of emerging securities enforcement systems? There are interesting indicators in light of the Brazilian example. These include, with regards to the securities regulator, (1) the adoption of a policy to prioritize enforcement; (2) modeling its structure after the SEC's "sole-entity" model,<sup>133</sup> including an independent Board of Commissioners; (3) undergoing a transformation into an enforcement-driven agency; (4) achieving considerable political independence; (5) establishing a stand-alone enforcement program with a mandate; (6) having access to an enhanced

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133. See Santana, *supra* note 12.

tool-kit to combat serious corporate wrongdoing in “real-time”; (7) the ability to settle; and (8) active partnerships with the criminal justice authorities; (9) with the industry; and (10) and with the international community.

These partnerships also speak to the development of a “multiple-enforcers” model reminiscent of developed markets. Despite the practical absence of private rights of action, the securities regulator has come to rely on collaboration with other law enforcement agencies, and has engaged in an active interplay with a sophisticated self-regulatory regime, sharing the burden of market surveillance with a quasi-governmental FINRA-like SRO.

Brazil’s recent experience with securities enforcement could well be a reflection of the path that lies ahead for emerging capital markets in today’s global arena.