

# INTERNATIONAL COMMERCIAL ARBITRATION IN BRAZIL

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## SUMMARY

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## • INTRODUCTION

For a long period of time, Brazil was not recognized as a country where arbitration played a central role as a dispute resolution method. This was also the time where the Brazilian economy, though relevant (since its GDP has been over the last twenty years among the 11<sup>th</sup> biggest in the world and almost the size of Canada's in absolute terms<sup>4</sup>), was based on the import substitute model and thus lacked external exposure. This was also a time of domestic hostility towards arbitration. These days are over. After president Cardoso's reforms in the 90's, the Brazilian economy became internationalized and domestic hostility towards arbitration decreased.<sup>5</sup> Brazil is now number four in the number of ICC Court of Arbitration cases (according to ICC arbitration report 2006)<sup>6</sup>.

However, the change of paradigm with respect to arbitration is not only a question of Economics and Commerce. It is also a matter of law. This article will explain what happened in the country with respect to arbitration from a legal point of view. This is because although economics is fundamental, it is not enough to bring efficiency in contracts and the market. This is the Coasean theorem, i.e, in an ideal world of zero transaction costs, parties can reach efficient solutions in spite of legal provisions.

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<sup>4</sup> <http://siteresources.worldbank.org/ICPINT/Resources/summary-tables.pdf>.

<sup>5</sup> TIMM, Luciano Benetti. The Transfer of Technology Direct Regulations in Brazil (Part I). *In Computer and Telecommunications Law Review.* , v.5, p.217 - 223, 1999

<sup>6</sup> ICC Statistical Report 2006, in ICC International Court of Arbitration Bulletin, vol. 18, issue 1, 2007, p. 05.

However, in a real world of transactions costs, the legal system does matter to efficient outcomes.<sup>7</sup>

Efficiency is the equilibrium situation in which one of the parties in a contract can improve its situation without making the other party worse off (Pareto efficiency) or improve as much as to abstractly compensate the harm of the other (Kaldor-Hicks criteria).<sup>8</sup> Literature suggests that often both parties, and at least one of the parties, will be better off resolving disputes through arbitration, rather than litigation. Parties are able to reach the most efficient solution through the bargaining process. The explanation for this probably lies in the decrease in transaction costs (due to the speediness of proceedings, the specialization of arbitrators). So if parties prefer an arbitration clause to a choice of forum clause, we can presume that it is more efficient for them.<sup>9</sup>

Given these assumptions, this paper seeks to explain the changes in Law that have allowed arbitration to play a major role in dispute resolution in Brazil. By Law we do not only mean the Law on the books – the provision of statutes and regulations of government bodies – but the Law in action – how courts interpret in practice those

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<sup>7</sup> Cooter explains: “Some transaction costs are endogenous to the legal system in the sense that legal rules can lower obstacles to private bargaining. The Coase Theorem suggests that the law can encourage bargaining by lowering transaction costs. Lowering transaction costs ‘lubricates’ bargaining. (...) We can formalize this principle as the normative Coase theorem: *Structure the law so as to remove the impediments to private agreements.* (...) It assumes that private exchange can allocate rights efficiently. (...)”. Cf. COOTER, Robert e ULEN, Thomas. *Law & Economics*. Boston, Addison Wesley, 2003, p. 93.

<sup>8</sup> COOTER, op. cit., p. 11 and 40. That is to say when the marginal cost equals the marginal benefit for each service or product.

<sup>9</sup> According to Shavell a “contract is said to be mutually beneficial or, in the language of economics, Pareto efficient, if the contract cannot be modified so as to raise the well-being – the expected utility – of each parties to it. We would suppose that contracts would tend to be mutually beneficial: if a contract can be altered in a way that this would raise expected utility of each party, we would think that this would be done”. Cf. SHAVELL, Steven. *Foundations of Economic Analysis of Law*. Cambridge: Harvard University Press, 2004, p. 293.

statutes and regulations. Brazil changed its federal law of arbitration and the Supreme Court confirmed it.

In many ways, the Brazilian experience mirrors the experience of the United States during the 20<sup>th</sup> Century, where there was initially a strong judicial resistance against arbitration, and then the passing of legislation (Federal Arbitration Act 1925, FAA, 9 U.S.C paragraph 1 *et seq.*), which was confirmed by a trilogy of cases within the United States Supreme Court (*Scherk v. Alberto-Culber Co*<sup>10</sup>, *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*<sup>11</sup>). The United States experience thus is illustrative of the Brazilian experience.

Naturally, the explanation for the increased acceptance of arbitration cannot be reduced to simply passing legislation and its confirmation by the courts. Rather, there are other legal and institutional reasons that will be explored in Part four of this paper. These reasons relate to lack of efficiency of the courts (time and expertise) and lack of confidence from foreign investors.

Part one of this paper will discuss the past legislation that created an obstacle to successful arbitration.

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<sup>10</sup> 417 U.S. 506 (1974). In *Scherk*, the Supreme Court decided, under the circumstances of the case, that an arbitration clause – that transfers the original jurisdiction of a court of justice to the arbitral tribunal – is valid even when related to an agreement to purchase securities of a company, in spite of the provisions of the Securities Act of 1933, particularly its paragraph 14 (which deems invalid any preclusion of the buyer to a legal remedy in court).

<sup>11</sup> 473 U.S. 614 (1985). In *Mitsubishi* case, The Supreme Court decided, under the circumstances of the case, that an arbitration clause is valid even when the subject matter of the dispute might involve antitrust law.

In part two, we will describe how the Federal Law 9307 of 1996 (Brazilian Arbitration Act, BAL) and the recent adoption by Brazil of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (hereinafter the “New York Convention”)<sup>12</sup> tackled the main problems.

In part three we will address the main precedents of higher courts with respect to the constitutionality and interpretation of the Federal Law.

In part five we will comment on some unresolved issues that still need to be addressed by the courts.

## **1. UNDERSTANDING THE LEGAL PROBLEMS OF PAST LEGISLATION**

### *1.1. Evolution of Arbitration in Brazil: legal reasons for its failure*

Brazil first adopted arbitration while it was still a Portuguese colony, since it was forced to implement all legislation that was enacted in Portugal. In 1824, with the proclamation of independence, a new constitution was created and arbitration was recognized in its article 160.<sup>13</sup> In the following years some laws made arbitration mandatory to some commercial cases.<sup>14</sup>

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<sup>12</sup> United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, ratified by Brazil in July 23<sup>rd</sup>, 2002 by the “Decreto” n. 4311.

<sup>13</sup> Jose Alexandre Tavares Guerreiro, *A Execucao Judicial de Decisoes Arbitrais*, 75 Revista de Direito Mercantil 31, 31 (1999).

<sup>14</sup> Article 411 of the “Regulamento n. 737” enacted in January 25<sup>th</sup>, 1850 and Articles 294 and 248 of the “Brazilian Commercial Code” enacted in 1850.

In 1867 a new law<sup>15</sup> revoked mandatory arbitration for certain commercial disputes, leaving the parties to choose arbitration as a method of dispute resolution if they so desired. This law was the first step of more than a hundred years of hostility to arbitration in Brazil. Following this law, the country adopted a very strong policy based on jurisdictional exclusivity of the courts (or state monopoly of jurisdiction).<sup>16</sup> This policy can be found in the most important codes and statutes that existed until the BAL was enacted, such as the Brazilian Civil Code of 1916 and in the Brazilian Civil Procedure Code of 1939 and 1973.<sup>17</sup>

Brazil signed and ratified<sup>18</sup> the Protocol of Geneva on September 24<sup>th</sup>, 1923. However, international treaties and conventions are internalized into the Brazilian Legal System with the same degree and level of a federal statute. Thus, the Protocol was superseded by several laws and statutes which were hostile to arbitration, such as the Civil Procedure Code in 1939 which preempted the validity of the aforementioned Protocol in Brazil<sup>19</sup>.

Late after, in 1981, as a result of the concern that legislation that was hostile to international arbitration decreased the amount of international trade in Brazil, the

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<sup>15</sup> Lei n. 1350, enacted in September 9<sup>th</sup>, 1866.

<sup>16</sup> Ricardo Alvarenga, *The 1996 Brazilian Law on Arbitration*, 10 World Arb. Mediation Rep. 340, at 341 (1999).

<sup>17</sup> Jurgen. Samtleben, *Procedimento Arbitral No Brasil - O Caso "Lloyd Brasileiro Contra Ivarans Renderi" Do Supreior Tribunal De Justica*, LXVII Revista da Faculdade de Direito da Universidade de Sao Paulo 185, 210. (1999)

<sup>18</sup> Ratified by the "Decreto 21.167" enacted in May 22<sup>nd</sup>, 1932.

<sup>19</sup> Alvarenga, *see supra note 6*, at 342; Hermes Marcelo Huck, *La Nouvelle Loi de L'arbitrage au Brésil*, Bull. Assoc. Suisse Arb. 570, at 572 (Switz. 1997).

Brazilian government decided to pursue legislation that would facilitate arbitration.<sup>20</sup> In the same year the government published a first draft of arbitration legislation seeking public comments. The draft was rejected by the majority of lawyers in the country. At that time most Brazilian lawyers were proud of the new Civil Procedure Code and rejected the draft on the grounds that it was inconsistent with the new code. With so much criticism, the draft was abandoned.<sup>21</sup>

The Libertarian Institute of Pernambuco made another attempt with a project called “Operação Arbiter” (Arbiter Operation) which designed a draft on the matter with public and private participation.<sup>22</sup> The draft was based on the New York Convention, the Panama Convention, the UNCITRAL Model Law on Arbitration and the Spanish Law on Arbitration.<sup>23</sup> On April 27, 1992 the project was finally sent to congress where it was discussed for four long years until it was enacted as law 9.307 on September 23, 1996. Just before the enactment of the BAL, Brazil signed and ratified The Inter-American Convention on International Commercial Arbitration<sup>24</sup>.

### *1.2. The legal problems of past legislation*

In Brazil, before the enactment of the BAL there were two main legal problems with both domestic and international commercial arbitration that restricted use of arbitration:

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<sup>20</sup> Irineu Stegner, *Arbitragem Comercial Internacional*, at 33 (LTR, São Paulo, 1998).

<sup>21</sup> *Id.*

<sup>22</sup> Alvarenga, *see supra note 6*, at 342.

<sup>23</sup> Maruska Guerreiro Lopes, *La Nouvelle Loi Brésilienne sur L'arbitrage*, 37 *Dalloz Affaires* 1, at 4 (Fr. 1997).

<sup>24</sup> Ratified on May 10<sup>th</sup>, 1996.

the non-recognition of the arbitration clause and the requirement of homologation (recognition) in Court.

### *1.2.1. Non-recognition of the arbitration clause*

Until the enactment of the BAL, arbitration clauses were unenforceable. Before, there was a requirement that if the parties preferred settling their dispute by arbitration instead of submitting the dispute to courts, the parties had to renew their agreement after the dispute had arisen.<sup>25</sup> If a party refused to comply with the arbitration agreement set out in a contract, courts in Brazil could only award damages for non-compliance of a contractual clause, but they would never compel the parties for arbitration.<sup>26</sup>

### *1.2.2. Homologation problem*

Homologation was considered the major problem for arbitration in Brazil before the BAL. According to the previous legislation in Brazil, an arbitral award was required to be “homologated” in a district court of justice in order to be fully valid, legally binding and enforceable. The homologation procedure was supposed to be done by means of a civil law suit with a right to defense, production of evidence, and, as any court proceeding bound by the due process of law clause, could take years to make a final decision. Therefore, all the advantages of arbitration were lost, especially speediness. Which party

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<sup>25</sup> Brest Fulkerson, *A comparison of Commercial Arbitration: The United States & Latin America*, 23 *Hous. J. Int'l L.* 537, at 554 (2001).

<sup>26</sup> Carlos Alberto Carmona, *A Arbitragem no Brasil, Em Busca de Uma Nova Lei*, 166 *Jurisprudencia Brasileira*, at 17-19 (1999).

would like to “retrial”<sup>27</sup> the issue in court, after an arbitration award from an ex-ante perspective – that is in the moment of drafting the agreement and chose for arbitration clause.

This was even worse for foreign awards that also required a recognition procedure by the Brazilian Supreme Court (even after homologation in a court at the place of arbitration). In most civil law jurisdictions, foreign arbitral awards need to be recognized previously in domestic courts to be enforced.

Hence, the “double homologation” problem (or double recognition procedure) for international arbitration awards, consisted in the recognition of the award by a court in the country where the arbitration took place and then in Brazil, by the Brazilian Supreme Court, “Supremo Tribunal Federal” (hereinafter STF). In this way, the STF would only submit the award to the tests of enforceability under Brazilian Law if that award was previously recognized by a Court in the country where the arbitration took place.<sup>28</sup> For instance, if an American party wanted to enforce in Brazil an arbitral award rendered in New York, it would need to recognize the award first in a New York court and then in Brazil.

This requirement was not only completely outdated, but also worked against the benefits of arbitration. The cost of arbitration would be increased by the obligation to

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<sup>28</sup> Guido F. S. Soares, *Arbitragens Comerciais Internacionais no Brasil: Vicissitudes*, 641 *Revista dos Tribunais* 38, at 47 (1989).

submit the award to the judiciary. In addition, time savings would be lost because of the slowness of the recognition process and the possibility of a special appeal.<sup>29</sup>

Those two main legal problems were tackled by BAL and also the recognition of the NY Convention.

## **2. THE BRAZILIAN ARBITRATION LAW: OVERCOMING THE COASEN PROBLEM**

The Brazilian intent in enacting the BAL was to adopt the most up-to-date rules of arbitration that were used in the world. For that reason, the Brazilian legislator found inspiration in more than five instruments, including the New York Convention and the UNCITRAL Model Law on Arbitration.<sup>30</sup> This clearly shows that the goal of the Brazilian government was to adopt the most recent theories in arbitration, and to follow the international practice.

The BAL addresses all topics of arbitration, and it is very similar to many arbitration statutes around the world, since Brazil is not the only country that has found inspiration in the provisions set by the UNCITRAL or by the New York Convention. The BAL has tackled the two main problems of the old legislation that was hostile towards arbitration. First, it made the arbitration agreement binding on the parties that had signed it (as provided in the New York Convention) and second, it released the parties from the need of the homologation of the arbitral award in domestic courts, considering an arbitral

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<sup>29</sup> *Id.*

<sup>30</sup> Guerreiro, *see supra* note 17.

award valid and enforceable *per se*, equal to a court award and (the BAL also equalized arbitrators and judges).

On one hand, Brazil recognized the autonomy and enforceability of an arbitration clause. A party that has signed such a provision cannot circumvent its force. Courts must direct the parties to arbitration in case of disputes in court with respect to litigation that falls within the scope of the arbitration clause. It is up to the arbitral tribunal to decide its jurisdiction (principle *kompetenz-kompetenz*). Moreover there is a remedy for a party to ask for specific performance to compel the other party to participate in arbitration if the clause does not give enough guidance to start proceedings (such those vague clauses stating that “disputes arising out of this contract must be resolved by arbitration”, without directions on which tribunal, which procedural law, etc).

On the other hand, considering the arbitral award valid and enforceable without the necessity of any homologation whatsoever, BAL released winning parties from the need to undergo the tiresome domestic homologation. Therefore, international awards did not need to be homologated in the court where the proceedings had taken place to be enforced in Brazil. Now, they only need to be recognized at the Superior Court of Justice, as any other kind judicial award from another country. In such a proceeding, there is no discussion on the merits of the case, the court only assesses if formalities were observed and if the public policy of the country is not offended.<sup>31</sup>

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<sup>31</sup> Like many other civil law jurisdictions, foreign awards (be it arbitral or court issued) need to be scanned by the Superior Court of Justice in a recognition proceeding. In this documentary trial (there is no hearings), the court will only assess formalities of the award (certified copies) and Brazilian Public Policy. It is

As a result of enacting the new law, Brazil removed the greatest barriers to domestic and international arbitration. *Bien entendu*, the BAL dispensed of the need for recognition by the foreign judiciary, but at the same time it maintained the requirement for the recognition of foreign awards by the Superior Court of Justice (Superior Tribunal de Justiça – STJ)<sup>32</sup> – as accepted by the New York Convention.

The legal criteria to assess the need for this recognition is the test of the place where the award was given. If the place of delivery of the award is from a country other than Brazil such as Mexico, U.S., France, England, China or Japan, it is an international arbitration and must be recognized in the STJ. If it was delivered in Brazil, it is considered a domestic arbitration in spite of the nationality of the arbitrators, the parties, or the language of the proceedings. To avoid problems, the best alternative is a contractual provision to have the award given in the place where the arbitration is to take place.

Finally, preliminary injunctions are allowed by the Law to be issued by arbitrators. They can even ask for the cooperation of courts for their enforcement. So the BAL is

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similar to a summary judgment, but might take several months. Once recognized, the collection of the award must be filled in a Federal District Court.

<sup>32</sup> Article 35 of the BAL states that: “To be recognized or executed in Brazil, the foreign arbitral judgment is subject solely to homologation by the Supreme Federal Tribunal.”

very liberal in permitting arbitrators to grant orders to the parties to make sure that the outcome of the case is enforced.

As a result of the new legislation, Brazil overcame the main legal barriers to developing its arbitration system and to boosting the use of arbitration within the country. However this does not mean that we might not foresee futures problems of at least some controversial issues, to be addressed latter on.

### **3. *LAW IN ACTION: THE FEDERAL LAWS IN MOTION***

#### *3.1. Constitutionality of the Brazilian Arbitration Law*

One of the first reactions after the enactment of the BAL was a movement to declare certain parts of the statute unconstitutional, since some lawyers found that some Sections, in special Sections 4 and 7, were inconsistent with the provisions of the Constitution that granted full access to courts<sup>33</sup>. Article 7 of the BAL states that courts have to compel arbitration, issuing a judgment that operates as a specific performance for arbitration, if the parties have failed to provide for the applicable procedural or substantive rules and no agreement is reached by the parties.

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<sup>33</sup> Mary B. Brusewitz, *Brazil Ceases Its Antipathy Toward ADR*, The National Law Journal, Section C (1996).

The issue of unconstitutionality of the BAL is past now. STF, in a leading case<sup>34</sup>, ratified the understanding that under the provisions of the BAL all those disputes that are considered arbitrable under Brazilian Law shall be directed to arbitration. STF also held that the BAL does not infringe art. 5, item XXXV of the Brazilian Constitution, which states that “the law will not exclude from the consideration of the Judiciary any lesion or threaten to any right”. The goal of this provision is to prevent laws that allegedly suppress the rights of citizens to resort to the judiciary and not to limit the private autonomy.<sup>35</sup>

This leading case is the result of a proceeding that recognized an arbitral award issued in Spain that was not homologated in Spanish courts. STF was about to give its first application of the BAL (at that time, STF had jurisdiction in foreign awards recognition. Since 2005 the Superior Tribunal de Justiça “STJ” has the jurisdiction). The constitutionality issue was raised incidentally by one of the Justices in the case who questioned whether Sections 4 and 7 of the BAL were overall constitutional.

On one hand, Justice Sepúlveda Pertence argued for the unconstitutionality of article 4, since it would characterize a “generic waiver, of an indefinite object, to the assurance of access to the jurisdiction” and thus not applicable to the case at hand<sup>36</sup>. On the other hand, Justice Nelson Jobim countered with the argument that the Constitution does not bar the parties from agreeing to other forms of settlement of disputes that may arise

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<sup>34</sup> STF case SE 5206. For a brief on the case in English see: <http://www.stf.gov.br/portal/jurisprudenciaTraduzida/verJurisprudenciaTraduzida.asp?tpLingua=21&id=280>

<sup>35</sup> Brusewitz, *see supra note 36*.

<sup>36</sup> Selma M. Ferreira Lemes. Litigation v. Arbitration in the Americas. In: [http://www.servilex.com.pe/arbitraje/colaboraciones/litigation\\_arb.html](http://www.servilex.com.pe/arbitraje/colaboraciones/litigation_arb.html). Accessed in December 2003.

within the scope of a certain agreement (principle of the freedom of contract). Justice Ilmar Galvão adds that :

*“the Brazilian judge cannot interpret the new law to make innocuous the provision that equalizes the clause, giving it effectiveness, even if by resorting to the judicial judgment, under penalty of showing to be insensitive to the changes that occurred in the same period in several laws, even because, including, it is in line with the international texts in force in Brazil, such as the Protocol of Geneva of 1923 and the Inter American Convention on Commercial Arbitration done in Panama”.*<sup>37</sup>

Moreover, Justice Ellen Gracie stated that:

*“denying the possibility that the commitment value to have full validity and give raise to the specific execution implies to privilege the defaulting party and denying the submittal to the quick way of dispute settlement, a mechanism for which it freely opted, upon the execution of the agreement where this provision was inserted. It is giving the defaulting party the power of voiding a condition that – given the nature of the involved interests – could have been deemed to be essential for the agreement.”*<sup>38</sup>

Moreover, Justices Celso de Mello and Marco Aurélio Mello had the same understanding, declaring the constitutionality of article 4 and, thus the constitutionality of the BAL in its entirety. As a result, by a majority, STF renders constitutional all the provisions of the BAL (In Brazil as in the U.S., Justices render opinions and the Court decides by majority).

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<sup>37</sup> *Id.*

<sup>38</sup> *id.*

### 3.2. The environment pro-arbitration in the Superior Court of Justice *post* STF ruling

The Brazilian Superior Court of Justice has been very conscious of its role in creating a nurturing environment for arbitration to develop. In its first case dealing with the enforcement of foreign awards, the STJ moved toward bringing Brazil in line with major western courts around the world. In Recognition Proceeding (Sentença Estrangeira Contestada, SEC 856/EX, May 18, 2005), the STJ recognized an English arbitral award made following an unsigned arbitration agreement. The court unanimously found that the award should be recognized, stating that the “requirement of acceptance of the arbitration agreement is satisfied where the party opposing recognition [of the foreign award] filed a defense in the arbitration proceedings, without at any time challenging the existence of the arbitration clause.”

In another leading case, Special Recourse (*RECURSO ESPECIAL*)<sup>39</sup> 712.566, the Superior Court of Justice accepted an arbitration clause in an international agency agreement even when it was signed before Federal Law 9307 from 1996 (which was a dramatic liberalization in favor of arbitration since in Brazil the agent is protected from the principal in domestic commercial agreements because Federal legislation considers that there is a lack of bargain power on sales representative agreements like consumers and tenant-landlord agreements in the U.S.).

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<sup>39</sup> American readers can translate it for *writ of certiorari*. Though it works a little bit differently in Brazil, it is a recourse for the highest federal court in the country, whose aim is to guarantee uniform interpretation of federal statutes. The interpretation of the Constitution is the Federal Supreme Court.

Those two leading cases demonstrate that the Superior Court of Justice is doing its homework and is applying Federal Law 9307 and the New York Convention according to the expectations and the need of international commerce which gives a further explanation for the explosion of international commercial arbitration in Brazil.

A few State Courts, like the Court of Appeals of Rio Grande do Sul still resist arbitration (unlike in the U.S., a Brazilian State Court must apply Federal Law and basically all contract law is regulated by Federal Laws, especially the Civil Code). However, these decisions are open to revision by the Superior Court of Justice through Special Recourse.

#### 4. OTHER REASONS FOR THE SUCCESS OF ARBITRATION

In Brazilian courts, litigation is highly subsidized by the government, creating incentives to litigate, in addition to the rule that the loser in court pays the winner's fees. Also, in the past the interest rates were too high and interest rates applied by courts (12% per year) were not enough to cope with the market interest rates, which also gave incentives to use trial as a form of speculation. On top of that, normally parties tend to be excessively optimistic about their chances of winning, making settlements hard to reach; but in Brazil this situation is worse due to the lack of binding precedents, which creates difficulties for lawyers to foresee the outcome of the trial.

There are also problems with the case docks being overloaded.<sup>40</sup> Though Brazilian courts are different from the majority of Latin America, because the Judiciary is independent (it has a proportion of the budget revenues of the government and judges are not appointed by the executive except in the Supreme Court, and are well paid), they are still slow compared to German or American Courts.<sup>41</sup>

For example, a survey conducted by Professor Prado from Fundação Getúlio Vargas, involving the State Courts of São Paulo (the richer in Brazil) in matters related to capital markets and corporate law evidenced that cases in this field take more than seven years on average to be fully litigated if they reach the highest court. The trial courts are the slowest, which give the parties the impression that the courts are inefficient.<sup>42</sup>

Brazilian courts might also be seen with defiance by Americans, Canadians and Northern Europeans, due to the tendency of oversimplification of Latin America and its countries (there are those that treat Brazil as being in the same category as Bolivia, Guatemala, Ecuador, Argentina, Chile, even though the latter countries' level of corruption is much higher. Though it is difficult to measure, the International Transparency attempted to create an index of corruption, which shows that for instance the corruption index in Chile

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<sup>40</sup> For a general overview of Latin America, see BUSCAGLIA, Edgardo. A quantitative assessment of the efficiency of the judicial sector in Latin America. *In International Review of Law and Economics*, vol. 17, 1997, p. 275. For a more accurate and precise assessment of Brazilian Judicial Power see *Court Performance around the world: a comparative perspective*, World Bank Technical Paper # 430, WTC430, 1999. For present figures, see the Report of the Brazilian National Council of Justice, *Justice in numbers*, [http://www.cnj.gov.br/images/stories/docs\\_cnj/relatorios/justica\\_numero\\_2005.pdf](http://www.cnj.gov.br/images/stories/docs_cnj/relatorios/justica_numero_2005.pdf)

<sup>41</sup> *Court Performance around the world: a comparative perspective*, World Bank Technical Paper # 430, WTC430, 1999

<sup>42</sup> PRADO, Viviane Muller; BURANELLI, Vinicius Correa. *Relatório de pesquisa de jurisprudência sobre direito societário e mercado de capitais no tribunal de justiça de São Paulo*. In *Cadernos Direito GV – Relatório de Pesquisa*, n. 09. São Paulo: FGV-EDESP, 2006, p. 27.

and Uruguay are similar to that of the US and Brazil would be more or less on the same level as India, China, and South Korea, and other smaller countries in Latin America might be closer to Africa.<sup>43</sup> Also, the level of corruption could be associated in the case of Brazil with the Executive Branch, which is much more dependent on corporations and wealthy individuals who pay for their campaign than the Judiciary (harder to capture).

An empirical study must be conducted but it is not difficult to guess that international companies that do business in Brazil (probably the bigger pie in the demand side for international commercial arbitration involving Brazil in ICC, though Brazilian multinationals are getting very involved in transnational business such as Petrobras (oil company), Vale do Rio Doce (mining), Gerdau (steel), Embraer (jets) probably prefer to have an arbitration in “reliable” countries such as France, Sweden, the U.S., Canada, and England.

Another contribution might be the suggestion of Dezalay and Garth about the American and British Law Firms’ taking over of the legal market around the globe.<sup>44</sup> If they are right, we can imagine that those firms would prefer to conduct the arbitration when they know the *lex arbitrii*. To have the arbitration in Brazil, though it would probably be cheaper and would achieve more or less the same result, those firms would have to rely

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<sup>43</sup> [http://www.transparency.org/policy\\_research/surveys\\_indices/cpi](http://www.transparency.org/policy_research/surveys_indices/cpi)

<sup>44</sup> See DEZALAY, Yves & GARTH, Bryant. The confrontation between the big five and big law: turf battles and ethical debates as contests for professional credibility. In *Law and Social Inquiry*, vol. 29. 2004, p. 615; DEZALAY, Yves & GARTH, Bryant. Merchants of law as moral entrepreneurs: constructing international justice from the competition for transnational business disputes. In *Law and Social Inquiry*, vol. 29. 1995, p. 27; DEZALAY, Yves et al. Global restructuring and the law: studies of the internationalization of legal fields and the creation of transnational arenas. In *Case Western Reserve Law Review*, vol. 44, 1994, p. 407. ENGELMANN, Fabiano. *Sociologia do campo jurídico: juristas e usos do direito*. Porto Alegre: Editora Sergio Antonio Fabris, 2005.

on Brazilian lawyers to control the proceedings. And this would imply costs and also lack of revenues. Moreover it is in the best interest of the client to have the arbitration take place in countries where courts are not hostile to private litigation.

## 5. FUTURE ISSUES

After the rough years following the enactment of BAL, the Brazilian government tried to show, once more, that Brazil is making all efforts to make the country more attractive to businesses who rely on arbitration, and to show by ratifying the New York Convention that the international standards in arbitration are also applied in Brazil. There are two main aspects to be discussed that relate to the recent ratification of the New York Convention by Brazil and both deal with grounds for refusal to recognize or enforce arbitral awards.

As aforementioned, many principles of the Convention were adopted in the BAL, even prior to the ratification by Brazil. Articles 37 to 39<sup>45</sup> seem to be a direct translation

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<sup>45</sup> Article 37. The homologation of a foreign arbitral "judgment" shall be requested by the interested party. The initial complaint should contain the requirements of procedural law in conformity with Article 282 of the Code of Civil Procedure and shall necessarily be accompanied by:

I - the original of the arbitral "judgment" or a duly certified copy, authenticated by the Brazilian Consulate and accompanied by an official translation;

II - the original of the arbitration agreement or a duly certified copy, accompanied by an official translation.

Article 38. Homologation may only be denied for recognition or execution of a foreign arbitral "judgment" when the defendant shows that:

I - the parties lacked capacity in the arbitration agreement;

II - the arbitration agreement was invalid according to the law to which the parties submitted themselves, or, in default of such showing, by virtue of the law of the country where the arbitral "judgment" was rendered;

III - there was no notification of the designation of the arbitrator or of the arbitration proceeding, or the principle of the adversary system was violated, making an ample defense impossible;

IV - the arbitral "judgment" exceeded the limits of the arbitration agreement, or it was not possible to

of articles IV and V of the New York Convention. They cover the issues of how to recognize and enforce a foreign arbitral award, and when the recognition and enforcement can be refused.<sup>46</sup>

### **5.1. Public Policy**

Although the principle in the New York Convention is to refuse enforcement of an award that goes against "the public policy of that country"<sup>47</sup>, there is no doubt that the intention of the drafters of the New York Convention was to create a pro-enforcement atmosphere for international commercial arbitration. This implies that the drafters intended to encourage a narrow construction of the public policy defense.<sup>48</sup>

The United States of America, following the New York Convention, established in its own courts the interpretative line that the recognition and enforcement of foreign arbitral awards should only be denied when it would cause the violation of the "most basic

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separate the part that exceeded it from that which was submitted to arbitration;

V - the institution of the arbitration was not in accordance with the arbitral submission or the arbitration clause;

VI - the arbitral judgment has not yet become obligatory for the parties, has been annulled, or, it has been suspended by a court of the country where the arbitral judgment was rendered.

Article 39. Homologation shall also be denied for recognition or enforcement of the foreign arbitral "judgment" if the Supreme Federal Tribunal determines that:

I - according to Brazilian law, the object of the dispute was not susceptible to being resolved by arbitration;

II - the decision offends national public policy.

Sole paragraph. Effective service on a party resident or domiciled in Brazil, in the form of the agreement to arbitrate or the procedural law of the country where the arbitration was carried out (including allowance of service by mail with unequivocal proof of receipt), shall not be considered offensive to national public policy, so long as the Brazilian party is assured ample time for the exercise of the right of defense.

<sup>46</sup> Gary B. Born, *International Commercial Arbitration*, at 795 (Kluwer Law International, 2001).

<sup>47</sup> Article V.2(b) of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

<sup>48</sup> *Parsons & Whittemore Overseas Co., Inc v. Société Général de L'Industrie du Papier*, 508 F.2d 969, at 974 (2d Cir. 1974).

notions of morality and justice."<sup>49</sup> Therefore, the public policy concept does not involve national political interests or their protection.

However in Brazil, the concept of public policy is still the subject of controversy. Public policy is an ambiguous concept, particularly in relation to international business. Fortunately, Brazil does not interpret this concept as a protective instrument for national political interests.<sup>50</sup> The literature tends to define it as a core structure of the country legal institutions and for the basic values of Brazilian society (for instance and above all the Constitution).<sup>51</sup> The case law narrow this broad concept and tends to identify it mainly with the respect of the due process of law clause (meaning proper notice of service, right to appear in trial, to have defense, to be heard, to produce evidence, etc)<sup>52</sup>.

Nevertheless we must remind readers that the Brazilian Constitution is “Programatic” (it intends to interfere and give directions to the economy), has social rights and tend to be very prolific (more than 200 sections dealing with all the basic aspects of the Law, such as labor law, consumer rights, environment, property, etc).<sup>53</sup> By this token is difficult to imagine that Brazilian courts would have the same liberal interpretation of the

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<sup>49</sup> *Id.*

<sup>50</sup> Carlos Nehring Netto, *The New Brazilian Arbitration Law*, I.C.C. Int'l Ct. Arb. Bull. (Special Supplement: International Commercial Arbitration in Latin America,1997)

<sup>51</sup> ARAÚJO, Nadia de. *Direito Internacional Privado: teoria e prática brasileira*. Rio de Janeiro: Renovar, 2003; BASSO, Maristela. *Contratos Internacionais do Comércio*. 3ª ed. Porto Alegre, Livraria do Advogado, 2002; STRENGER, Irineu. *Contratos Internacionais do Comércio*. São Paulo, Revista dos Tribunais, 1986.

<sup>52</sup> STF, cases SE 2.582, SE 5.418, SE 3.989, SE 4.013, SE 3.886, all of them found in the site [www.stf.gov.br](http://www.stf.gov.br).

<sup>53</sup> See <http://www.v-brazil.com/government/laws/constitution.html> for the full text in English.

Convention than the American Courts (for instance consumer law, labor law tend to be considered as a matter of public policy in Brazil and thus non arbitrable issues).

### ***5.2 Disputes not capable of settlement by arbitration under Brazilian law***

Finally, Brazil has a very strict policy on matters that can be arbitrated. According to the New York Convention article V:

*“2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:*

*(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country”*

This means that many awards cannot be enforced because the subject matter of the award cannot be arbitrated under Brazilian law. Thus, arbitration can only be used to resolve disputes "relating to arbitrable patrimonial rights," which refer to alienable property rights, in accordance to article 1 of the BAL.

With the exception of some employment contracts, matters of commerce can be arbitrated under the United States Federal Arbitration Act ,<sup>54</sup> As the Commerce Clause of

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<sup>54</sup> Federal Arbitration Act, 9 U.S.C. § 1 (1999).

the United States Constitution<sup>55</sup> is read broadly,<sup>56</sup> most civil matters are considered arbitrable in the United States.

With respect to government contracts, the situation in Brazil is very different from that in the U.S. When the government enters into a contract in a position of *ius imperii*, i.e., in his position of representing the authority of the state, arbitrability is more difficult to be admitted. However leading cases of higher courts already accepted arbitration agreements signed by state-owned companies when they act in the marketplace as any other private party (*ius commercii*).

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<sup>55</sup> U.S. Const. art. I, § 8, cl. 3.

<sup>56</sup> *Wickard v. Filburn*, 317 U.S. 111, 124-25 (1942).

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