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Protectionist Amendments to Peru's Arbitration Law Disguised as Transparency

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On January 24, 2020, Peru enacted the Emergency Decree No. 020-2020 (the "Decree"), published in Peru's Official Gazette, El Peruano.[1] The Decree amends Peru's Legislative Decree No. 1071 (the "Arbitration Law"), in force since 2008,[2] to provide protections to any arbitration in which the Peruvian Government is involved. The Decree's changes are, in fact, protectionist measures to shield the government from certain arbitrations—such as *ad-hoc*—and are a problem for the arbitrators working on cases in which the state is a party.

As an arbitral jurisdiction Peru is *sui generis*. Peru's state procurement and contracting system obligates all controversies arising under a contract signed by the state to be submitted to arbitration. No other jurisdiction in the world has a system like this. This also means that Peru's system requires two arbitration laws instead of just one. A general law providing general principles and tailored for private arbitration and a special law in which the arbitration of government contracts is regulated. The former is the Arbitration Law, cited above, and the latter is the Government Contracting Law (the "LCE").[3] The former is of supplementary application to the latter.

The Decree amended the Arbitration Law and not the LCE, which by reasons we will discuss in this post is a legislative mistake which will create problems for all involved in the system. In addition, the Decree is, overall, a protectionist, misplaced, poorly penned piece of legislation.

The problems begin very early on in the Decree. The fourth recital recognizes the above described duplicity in the Peruvian system by stating that the Arbitration Law is "ideal for arbitration between private parties." Inexplicably, the recital states that the Arbitration Law is "not well suited" for arbitrations in which the state is a party; an obvious conclusion as the LCE governs those arbitrations. The recitals then go on to declare the purpose of the amendments as measures to "assure transparency" and, consequently, prevent corruption. However, the recitals also state that the measures are meant to prevent "situations which may affect the interests of the State and cause serious economic damages to the country" acknowledging its protectionist intent.

Some of the changes are justified and advance legitimate government interests. However, these changes are misplaced, and do not assure transparency or prevent corruption.

Analyzing the Decree's provisions shows that it modifies articles 7, 8, 21, 29, 51, 56, and 65 of the

Arbitration Law and incorporates a new article 50-A. For purposes of this post we will focus on articles 7, 8, 21, and 29, and in the Complementary Provisions which impact these or other articles.

Article 7 refers to the distinction between *ad hoc* and institutional arbitration and clarifies that *ad hoc* is the default process in case the parties failed to choose an institutional arbitration. The Decree changes this principle and bans *ad-hoc* arbitration in cases in which the state is a party. The only exception are cases with an amount in controversy below 10 Tax Units or approximately US$13,000. This excludes most cases filed against the state.

While the Arbitration Law is of supplementary application to the LCE, which limits *ad-hoc* arbitration, the LCE did not limit it to the extent the Decree has. In fact, *ad-hoc* arbitration now may be subject to two limitations, instead of just one. Under the LCE, *ad-hoc* arbitration is subject to the reference value of the contract (max US$1,5Mio); under the Decree, the limit will also depend on the amount in dispute (max US$13K). Therefore, it becomes riskier to undertake an *ad-ho*c arbitration because a judge may vacate the award based on either of these limits. Further, arbitrators will have serious problems when deciding whether to apply the LCE (special law—mandatory) or the Arbitration Law (general—supplementary) when they find contradictions between them; *e.g.* limitation periods to file for arbitration and diverging provisions on parties right to refile arbitration claims.

Another concern is the possible limited access to institutional arbitration. While institutional arbitration is perfectly fine and the Arbitration Centers of the Lima Chamber of Commerce, AMCHAM Peru, or the Universidad Católica provide excellent rules and administration, the implicit intent of the state is to create its own arbitral institution. Hidden in the First Complementary and Final Provision of the Decree is a mandate to the Justice Ministry to create the National Registry of Arbitrators and Arbitration Centers-RENACE (acronym in Spanish). This replaces the already existing National Registry of Arbitrators-RNA-OSCE (acronym in Spanish). We anticipate that the government will mandate that all domestic investor-state arbitrations be conducted by arbitrators registered in RENACE. RENACE and the existing State's Contracting Supervisory Body-OSCE (acronym in Spanish) will become the only institution able to manage government arbitrations. Bear in mind that the requirements to register as an arbitrator in RENACE are so steep that very few professionals will ever qualify; thus, RENACE will be a closed "club" of state approved arbitrators.

The Decree also changes Article 8, addressing judicial processes in aid of arbitration. These changes now require that a judge imposing provisional measures, such as an attachment or injunction, obtain security for such remedy; such was not the case prior to this amendment. The security must be financial, *e.g.* bond, letter of credit, or similar, filed with the judge before issuing the measure. While such requirement is not unreasonable, there is no alternative to a financial security and limits are needed to assure that the security is not abused. The government has created a strong shield against provisional measures as the contractor will have to have enough credit ability to obtain a facility for a provisional measure. Also, the government may try to collect on the security even if the provisional measure did not create any quantifiable damage. Moreover, these changes create internal ambiguities within the Decree. Specifically, the paragraph added states that "the amount of the security is established by […] the arbitral tribunal to whom the measure is requested." This contradicts the preceding paragraph which provides that provisional measures are issued by judges; it does not mention arbitrators. Articles 47 or 48 of the Arbitration Law would have been better places for the requirements of measures issued by arbitrators. Regardless of who should issue the measure, which will create confusion and delay, the amount of

the security could be as high as the claimed amount; it is customary for judges to link the security to the claim, rather than to a possible impact of the measure.

Following is Article 21. This refers to certain individuals' capacity to act as arbitrators. The original text of the Arbitration Law excluded government officials. The Decree further limits this to any individual who may have, directly or indirectly, an interest in the outcome of the dispute. Specifically, the Decree excludes all those who "previously acted in the specific case *sub judice*, either as an attorney for any of the parties, as an expert; or anyone who has personal, labor, economic, or financial interests which may conflict with the office of arbitrator, whether as lawyer, expert, and/or professional in other subject."

This is an attempt to eliminate the risk of bias or conflict of interest from arbitration panels. The effort will prove futile. As Professor Khaneman concluded in his studies of heuristics, biases are always present in decision making.[4] Those biases are based on deeply engrained, frequently unrecognized, factors. Stearns-Johnsen recognized that "your arbitrator … is biased. Litigators seek an unbiased panel when what they should really do is to understand that no panel … will ever be without bias. Everyone has biases … explicit and implicit … product of our culture, our surroundings, our innate preferences."[5] This, however, does not have to be an impediment for arbitral decision-making. Doak Bishop calls this the intuition that arbitrators have developed "over years of experience."[6]

Instead, conflicts of interest are and should always be addressed through disclosures. The very conflicts the government wants to use to disqualify arbitrators under the Decree, should be disclosed during the arbitrator selection process. It should be during the vetting that those conflicts are addressed; and may be waived by the parties. It would have been better to implement mandatory disclosures, with a structure like the IBA Guidelines on Conflicts of Interest in International Arbitration. Such guidelines provide for a tried-and-true system and reliable instruction for addressing conflict of interest, instead of a general and ambiguous disqualification rule.

Finally, the Second Complementary and Final Provision of the Decree is concerning. Such provision stipulates that the drafting of an arbitration clause is a multi-department process. The drafting responsibility rests on the contracting government unit and in the attorney general's office. This multi-layered process will interfere with contract negotiation and delay investment.

In conclusion, Peru's government did not successfully amend the Arbitral Law. The Decree's changes are either (i) a failed attempt at protectionism; (ii) misplaced, as these should have been included in separate legislation, such as LCE; or (iii) wholly unnecessary. The Decree's only accomplishment is to create ambiguities and ultimately jeopardize the effectiveness' of a system that has worked successfully for over 10 years.

References

?1 Emergency Decree Modifying Legislative Decree Nº 1071, Legislative Decree Norming Arbitration, Emergency Decree No. 20-2020 (Jan. 24, 2020) (Peru).

?2 Legislative Decree Regulating Arbitration, Legislative Decree Nº 1071, (June 28, 2008) (Peru).

?3 Consolidated and Organized Text of the Government Contracting Law, Supreme Decree Nº 082-2019-EF (Mar. 13, 2019) (Peru).

?4 DANIEL KHANEMAN, THINKING, FAST AND SLOW (2011).

?5 Joan Stearns Johnsen, Why Your Arbitrator is Biased, ABA Practice Points, https://www.americanbar.org/groups/litigation/committees/alternative-dispute-resolution/practice/2015/why-your-arbitrator-is-biased/.

?6 Doak Bishop, Lunch Presentation: The Quality of Arbitral Decision-Making and Justification, 6 World Arbitration & Mediation Review 801, 811 (2012).

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