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Transmission of Arbitration Agreements By Subrogation: The Newfound Brazilian Approach

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In a landmark decision rendered on May 15, 2019, the Brazilian Superior Court of Justice rejected the argument that transmission of an arbitration agreement via subrogation violated public policy. The Court thus gave full effect in Brazil to a foreign arbitral award resulting from a transmitted arbitration agreement. The decision sets the "law of the land" on a highly-debated issue in this country and abroad.

The issue appears quite often in insurance disputes. By settling a claim raised under an insurance contract, the insurer is put in the position of the insured and thereby becomes vested with the power to enforce the insured's rights against third parties. In technical terms, the insurer *is subrogated* in the rights of the insured against the party who caused the damage that gave rise to the insurance payment.[1)] Against this background, the question put to the Superior Court of Justice was the following: where the contract between the insured and the third party contains an arbitration agreement, once the insurer pays the indemnification, is the insurer bound by such arbitration agreement to assert his/her rights against the third party? The Superior Court of Justice's answer was yes.

The judgment was handed down in the context of a request for recognition of an ICC foreign arbitral award. In declaring that the third party was not at fault for the damages, the arbitral tribunal held that it had jurisdiction over the insurance company, despite the latter's contention that it was not a party to the contract and, therefore, was not bound by the arbitration agreement.

The recognition of the arbitral award inspired controversy amongst the Justices of the Superior Court of Justice. Justice Noronha spearheaded opposition to the recognition, arguing that transmission of the arbitration agreement by subrogation would be in violation of public policy – grounds for denial of recognition under Art. V.2.b of the New York Convention, reproduced in Art. 39, II, of the Brazilian Arbitration Act.

In brief, Justice Noronha was of the opinion that (*i*) the arbitration agreement is procedural in nature, and is not encompassed within the "*rights and actions*" transferred via subrogation; (*ii*) subrogation encompasses "*rights and actions*", but not the obligations undertaken by the insured party; (*iii*) an arbitration agreement is *intuitu personae* and therefore its transmission cannot be presumed; (*iv*) consent to arbitration must be express. Justice Noronha's reasoning was ultimately rejected by the majority.

In particular, the Reporting Justice, Og Fernandes, thoroughly examined the interpretation to be given to the concept of public policy as a ground for refusing to recognize foreign arbitral awards. In his view, in ascertaining whether a violation of public policy has occurred, the Superior Court of Justice must ask whether the foreign award is (*a*) absolutely incompatible with (*b*) the fundamental principles of (*c*) national public policy. In other words: is the foreign award entirely repulsive in light of public policy? Justice Og Fernandes answered the question in the negative –transmission of the arbitration agreement by subrogation would not be contrary to the fundamental principles of Brazilian public policy, which made it unnecessary for him to delve into the arguments for or against the transmission itself.

Concurring with the Reporting Justice, Justice Nancy Andrighi dug deeper into the analysis of transmission of arbitration agreements by subrogation. She took the position that arbitration agreements have a dual procedural-substantive nature and, therefore, can indeed be subject to transmission. Moreover, upon being subrogated in the insured's rights and actions, the insurer effectively steps on the former's shoes and binds itself to the underlying source of rights and obligations in all of its "limits, defects, qualities, terms and conditions". Finally, an obligation is only *intuitu personae* where it would not have been undertaken were it not for the individual characteristics of the obligor. In Justice Andrighi's view, this consideration does not apply to an arbitration agreement whose terms are generic and equally applicable to both contracting parties, regardless of their personal characteristics.

The award was thus recognized by a 9-3 majority opinion. This groundbreaking decision is in line with the stance adopted by courts in different jurisdictions (*e.g.*, United States, England and France), and once again reinforces Brazil's position as the "belle of the ball" within the international arbitration community. The judgement will serve as a compass in cases to come, and lay another brick in the pro-arbitration path that has been paved by the Superior Court of Justice and the Brazilian Judiciary as a whole.

References

?1 Brazilian Civil Code, Art. 786: “Upon payment of the indemnity, the insurer is subrogated, up to the amount of the indemnity, in the rights and actions that the insured has against the party that caused the damage.”

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