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# Brazil Allows Arbitration in Public Contracts in the Port, Road, Rail, Waterway And Airport Sectors

Orlando Cabrera (Hogan Lovells) · Saturday, October 12th, 2019

One effective way to manage risk allocation and especially political risk in state contracts consists of delegating dispute resolution and contract interpretation to arbitrators. With the aim to entice more private investors to develop infrastructure, Brazil has taken one positive step to expressly allow arbitration in public contracts concluded in these sectors.

On 20 September 2019, the President of Brazil issued Decree No. 10.025 (Decree). This Decree provides for arbitration within the port, road, rail, waterway and airport sectors to settle disputes between the Union or the entities of the federal public administration, and concessionaires, sub-concessionaires, lessees, permit holders and port operators (Contractors). Briefly, this post describes the eight most prominent features of this Decree.

**Matters of Dispute Capable of Settlement by Arbitration**

According to the Decree, disputes concerning "available property rights" (*direitos patrimoniais disponíveis*) may be subject to arbitration (Art. 1). This is consistent with the Brazilian *lex arbitri* that allows the public administration to use arbitration to settle disputes over "available property rights". Available rights are those which a party may renounce.

This approach has also been taken by other Latin-American jurisdictions like the Dominican Republic. Under the Dominican *lex arbitri*, the Dominican State may submit to arbitration "matters of free disposal" or "freely available matters" ("*materias de libre disposición*"). Also, in *Commisa v. Pemex*, the Eleventh Collegiate Court in Civil Matters in Mexico City interpreted that arbitrators may rule on matters of free disposal ("*libre disposición*").

The terms "available property rights" may be subject to diverse interpretations. However, the Decree opted to provide certainty regarding those available property rights. As such, the Decree provides that available property rights include: (1) issues related to the economic-financial balance of contracts; (2) the calculation of indemnities arising from the termination or transfer of the partnership agreement; and (3) the breach of contractual obligations including penalties. (Decree no. 10.025, Art. 2) This approach provides certainty as parties to arbitration know beforehand which matters may be capable of settlement by arbitration, and limits the judiciary's discretion to interpret available property rights in a restrictive manner that entirely precludes every matter from

arbitration.

## General Rules for Arbitration

The Decree provides certain general rules applicable to these arbitrations: (1) the arbitral tribunal shall apply Brazilian law, arbitration in equity is expressly forbidden; (2) arbitration shall be carried out in Brazil and in Portuguese; (3) information related to the arbitral proceedings shall be public except for the protection of trade secrets; (4) institutional arbitration will be preferred over ad hoc arbitration. Ad hoc arbitration will be accepted when it is duly justified, although the Decree does not specificy when this is granted; (5) only arbitral institutions previously approved by the Federal Attorney's Office will be chosen to settle the dispute. (Decree no. 10.025, Art. 3)

## Approved Arbitral Institutions

The Federal Attorney's Office will approve arbitral institutions that (1) are operating as such at least for three years; (2) are reputed for their experience and capabilities in conducting arbitral proceedings; and (3) have their arbitral rules translated into Portuguese. (Decree no. 10.025, Art. 10) This requirement seems to secure certain degree of competence when opting for an arbitral institution and it makes sense to have the rules translated into Portuguese as this will be the language of the arbitration.

The arbitration agreement may stipulate that the Contractors will indicate the arbitral institution from the list of approved institutions. The public administration can object the Contractor's decision within fifteen days. In this case, the party requesting the arbitration shall appoint another approved institution within fifteen days from the date of the objection. (Decree no. 10.025, Art. 11) The Decree does not specify how many times the public administration can raise objections. To avoid these potential objections and delays parties should designate an arbitral institution in the arbitration agreement.

## Arbitration Clauses Formalities

When the contracts contain an arbitration clause, (1) this clause will be highlighted in the contract; (2) it shall comply with the arbitrability matters and the general rules for arbitration previously discussed; (3) it shall define if the arbitration will be institutional or ad hoc; (4) it shall stipulate the place of arbitration and that parties will comply with the provisions of the Decree; (5) if the arbitral institution is not chosen, the clause shall provide for the criterion and procedure for choosing the approved institution. Contracts that do not contain an arbitration clause may be amended to include this clause. (Decree no. 10.025, Articles 5 and 7)

The federal public administration will previously assess the benefits and pitfalls of entering into arbitration agreements when an arbitration clause is absent in a contract. Arbitration will be preferred when (1) the disputes are based on predominantly technical aspects; (2) the delay in the final settlement of the litigation may cause damages to the proper performance of the public services or the infrastructure's operation or could inhibit investments considered as

priorities.(Decree no. 10.025, Art. 6) Nonetheless, the Decree does not impose an obligation on the federal public administration to agree to arbitration under the above scenarios.

**Time**

The arbitral proceedings must observe the following: (1) the respondent shall have at least sixty days to answer the request for arbitration; (2) to issue the final award, arbitrators have twenty-four months from the terms of reference's date. This time to issue the final award may be extended only once if the parties agree so, and that period must not exceed forty-eight months. (Decree no. 10.025, Art. 6) In practice, arbitral institutions frequently grant extensions to answer the request for arbitration. Probably, the sixty days to answer the request for arbitration seem plausible when parties agree to *ad hoc* arbitration. The second provision giving arbitrators two years to render the award and the extension may be a good incentive to conduct the proceeding in an expedite fashion. However, not all arbitration rules contain terms of reference. Thus, to comply with the Decree and to start the clock for rendering the award, arbitrators and parties will need to agree to terms of reference in all arbitrations, including those where the rules do not provide for terms of reference.

**Costs**

The Contractors shall advance the costs of the arbitral institution and the arbitrators' fees, and when applicable, these costs shall be reimbursed in accordance with the final resolution in the arbitral proceeding. (Decree no. 10.025, Art. 9) Although this requirement deviates from international standards, it may be helpful to discourage any frivolous claims.

If each of the parties partially loses, they shall bear the arbitration's costs proportionally. On the other hand, winning parties may recover attorneys' fees from their counterparts, but only *special contingent fees* (*honorários sucumbenciais*) not *contractual attorneys' fees* (*honorários contratuais*). To determine these special contingent fees, the Decree mandates the application of special rules on counsel's fees set by the the Civil Procedure Code. Article 85 of this Code sets a scale to grant counsel's fees, the percentage varies depending on the amount awarded.

The parties shall be responsible for the expenses resulting from hiring technical experts. These expenses shall not be reimbursed at the end of the arbitral procedure. If the parties agree otherwise, the Contractor shall advance the costs related to the production of expert evidence, including the expert's fees. (Decree no. 10.025, Art. 9)

**Arbitrators**

Arbitrators must comply with the following: (i) to have civil capacity; (ii) to know the subject-matter of the dispute; and (iii) to be free from conflicts of interests set forth in laws, rules or international standards. (Decree no. 10.025, Art. 12) These provisions give substantial leeway to choose international arbitrators, within international parameters. Notably, the Decree permits the potential use of the IBA Guidelines on Conflicts of Interest in International Arbitration to assess any conflicts of interest.

**Representation and Experts**

The Federal Attorney's Office will represent the Union and the legal entities of the Public Federal Administration. Also this Office can request expert opinions to the public officers in the arbitrations. (Decree no. 10.025, Articles 13 and 14)

**Comments**

This Decree provides confidence to investors willing to develop Brazilian infrastructure. True, the Decree sets protectionist requirements as having the seat of arbitration in Brazil, and to conduct the proceedings in Portuguese before an approved arbitral institution. Nevertheless, these requirements do not seem to compromise the legitimacy of the arbitration; quite the opposite, having a list of approved institutions protects public interest by securing the needs of the state. For instance, having the arbitration rules translated into Portuguese is aligned with the need to conduct the arbitration in this same language. Also, the Decree seems to safeguard public interest by limiting the scope of arbitration, and by setting transparency provisions. Requiring Contractors to advance costs may be burdensome but decreases the possibility to advance frivolous claims. Overall, the provisions appear more beneficial than harmful, and investors having a claim with legal merit will prefer to start arbitration within the parameters of the Decree than to succumb to lengthy judicial procedures.

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