Kluwer Arbitration Blog

CBAr 22nd International Arbitration Conference: Business Contracts and Party Autonomy in Times of Instability and Uncertainty

Maria Luiza Mayr Maia (Lauro Gama Advogados) · Saturday, October 28th, 2023

On the final day of the CBAr 22nd International Arbitration Conference, the main theme discussed was party autonomy in business contracts, especially amidst scenarios of instability. At a first glance, one might wonder why a specialized conference would tackle such an elementary topic. However, as one of the panelists insightfully emphasized, revisiting the foundational tenets of any discipline, no matter how apparent, is essential to ensure its proper application.

The first panel addressed "Arbitration and Contractual Imbalance." It was conducted by Giovanni Ettore Nanni (Nanni Advogados, Partner), Mariana França Gouveia (VdA, Partner), and Christoph Brunner (Brunner Arbitration, Partner), and moderated by Rodrigo Garcia da Fonseca (FSL Advogados, Partner).

A discussion between economist Gustavo Franco (former President of the Brazilian Central Bank) and arbitrator Maurício Almeida Prado (MAP Negotiation and Arbitration, Partner) ensued, dealing with "Business Contracts and Dispute Resolution in Times of Instability," particularly in the Brazilian context.

(Non-) Intervention in Business Contracts: The Case of Brazil

Giovanni Ettore Nanni's thoughts on business contracts weave through his take on the Brazilian Economic Freedom Act. Introduced in 2019, this law emphasized the importance of economic freedom, good faith, and the respect for contracts. It revised the 2002 Brazilian Civil Code to expressly provide for **(a)** the principle of minimal intervention; **(b)** the exceptional nature of contractual revision; **(c)** the presumption of parity in business contracts; **(d)** the possibility for parties to establish parameters for contractual interpretation, revision, and termination; and **(e)** the respect for the risk allocation agreed upon by the parties.

Opinions on the Brazilian Economic Freedom Act swing between admiration and skepticism. While some hail it as pivotal touchstone in the Brazilian legal system, others, such as Prof. Nanni, feel the text is devoid of technical scrutiny, especially since the new provisions do not add much to the Brazilian Civil Code framework.

As Prof. Nanni highlighted, the Brazilian legal system already considered business contracts as forged between parties in a position of parity. In the business context, parties assume the risks and arrange a complex contractual design to achieve their ultimate goal, profit. They self-regulate their interests and allocate risks, ultimately trying to avoid third-party intervention in their relationship. Together with the well-established principle of *pacta sunt servanda*, this logic reinforces why, in Prof. Nanni's view, contracts must always be considered.

Considering the evolving complexities of business contracts, Prof. Nanni argues that judges and arbitrators should refrain from intervening in such contracts. Since parties allocated the risks at the outset, the imbalance should be assessed at the limit of its exceptionality, always factoring in the specifics of each case. According to him, arbitration in Brazil has traditionally adhered to the principle of non-intervention, ensuring that contracts' original terms are respected.

However, this stance might not be universally adopted. There remains an inclination among state courts to meddle in contracts, often exceeding their role and sidelining original agreements. That is why the Brazilian Economic Freedom Act might be important after all. Though its provisions might seem rudimentary for arbitrators, arbitration lawyers, and academics, Prof. Nanni believes it is better to legislate the obvious to make it obvious to everyone.

Impossibility and Supervening Imbalance in Practice

While things might seem straightforward in theory, the practice is far more complex. As panelist Mariana França Gouveia observed, business relations are affected in many unexpected ways, such as the COVID-19 pandemic, the war between Russia and Ukraine, global inflation, the obstruction of the Suez Canal, the drought in the Panama Canal, and so on.

These inevitable occurrences, which are beyond the control of the parties, can fundamentally affect the performance of the agreement, either by rendering its fulfilment untenable (impossibility; force majeure) or disrupting the foundational assumptions that informed the parties' contractual decisions (supervening imbalance; hardship).

After exploring various legal systems, [1)] Prof. Gouveia discerned a near universal inclination (or struggle): while recognizing these external impacts, there is an earnest effort to shield contracts from their fallout. That is why exempting parties from performance is an exception; contracts should, as far as possible, be preserved.

Through an array of case studies, [2)] Prof. Gouveia further elucidated the application of this logic by both state courts and arbitral tribunals. Typically, the mere emergence of an unanticipated event does not exonerate a debtor from their obligation. The focus, instead, is on identifying whether there is a causal connection between the event and the debtor's non-compliance.

To some extent, Prof. Gouveia concurs with Prof. Nanni that adjudicators tend to adhere to established contractual terms. They aim to strike a balance between the sanctity of contracts and the flexibility needed in exceptional circumstances. As Prof. Gouveia highlighted, this approach is crucial to ensuring some certainty for economic agents and to assure them that their risk allocation will be considered.

The Duty to Renegotiate As a Possible Solution

A way to balance these two extremes was precisely the highlight of Christoph Brunner's lecture, which focused on the duty to renegotiate in hardship situations, absent a specific clause to that effect. As others pointed out, parties to business contracts usually have an interest in working out their differences and avoiding intervention. Whether parties can be forced to renegotiate, however, is an entirely different (and controversial) topic. [3)]

In general, the duty to renegotiate strives to encourage parties to find their own solutions and to minimize the intervention by tribunals in the contracts. A notable example is the provision of article 1,195 of the French Civil Code, which stipulates that "if a change of circumstances that was unforeseeable at the time of the conclusion of the contract renders performance excessively onerous for a party who had not accepted to bear such risk, that party may ask for a renegotiation of the contract to its contracting partner."

However, Prof. Brunner draws attention to the possibility of the duty to renegotiate extending (and being even more effective) into the litigation phase. Drawing from past experiences, [4)] he posited that tribunals could render interim decisions on preliminary issues, ushering parties to the negotiation table. If these tribunal-directed renegotiation falter, they could resort to the final offer rule, according to which parties are requested to present a final offer, one of which will be accepted by the tribunal.

This could arguably be considered an intervention by the tribunal. Regardless, as Prof. Brunner suggests, parties' participation in shaping solutions is definitely a better alternative than an outright intervention by adjudicators. To that effect, Prof. Brunner echoes Prof. Gouveia that hardship situations call for adaptable legal outcomes. In particular, the duty to renegotiate emerges as a legal framework for tribunal-guided renegotiations during a dispute to minimize court interference and preserve party autonomy.

Business Contracts and Dispute Resolution in Times of Instability

If the previous panels focused on the eminently legal aspects of hardship and the intervention of arbitrators in business contracts, the chat between renowned arbitrator Mauricio Almeida Prado and prestigious economist Gustavo Franco (one of the architects of the Plano Real, a set of measures introduced to curb hyperinflation in Brazil during the 1990s) merged the realms of law and economics to put a closure to the Conference.

According to Prof. Franco, stability – which underlies the entire discussion – is a term with multiple meanings. In the contemporary Brazilian context, stability is essentially synonymous with controlled inflation. According to him, however, monetary fluctuations are inherent even in stable settings. The real challenge for economists lies in discerning what would be considered a 'normal' fluctuation in a world without a uniform monetary standard.

Both Mr. Prado and Prof. Franco concur that contracts can be a way to shield parties from these fluctuations. A testament to this is the common contractual provision in Brazil, deeply rooted in the

nation’s tumultuous relation with hyperinflation, which stipulates a monetary correction index to adjust prices for inflation.

But contracts cannot foresee everything. As Prof. Franco underscored, referring to economist Frank Knight, risk and uncertainty, though similar, are not the same. While risk pertains to scenarios where future outcomes can be probabilistically forecasted (and hence insured, mitigated in the contract, and integrated into the economic transaction), uncertainty stands apart. Since there is no statistical basis to estimate the probabilities of uncertain future outcomes, there is a limit to what contracts can foresee.

Still, there is a consensus between the two that arbitration seems to be a good forum for deciding such cases. Although drawing the line between foreseeable risk and sheer uncertainty is not straightforward, arbitral tribunals strive to find the right balance between party autonomy and exceptional intervention, always bearing in mind that contracts should, as far as possible, be preserved.

Conclusion

The panelists provided an insightful exploration of party autonomy in business contracts in the face of uncertainty. Prof. Nanni, Prof. Gouveia, and Prof. Brunner examined foundational legal principles, practical challenges, and the potential ways out. Under an economic perspective, the dialogue between Mr. Prado and Prof. Franco highlighted the limitations of contracts in addressing uncertain events. The debates on the last day of the Conference emphasized the delicate balance arbitrators must find between upholding party autonomy and intervening during exceptional circumstances in an ever-evolving economic landscape.

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References

?1 Prof. Gouveia examined the legal landscape in Portugal (Portuguese Civil Code, Articles 437 and 790), in Brazil (Brazilian Civil Code, Articles 317, 478, and 393), in Germany (German Civil Code, Articles 275 and 313.1.3), in England (British Electrical and Associated Industries (Cardiff) Ltd v. Patley Pressings Ltd [1953]; Fibrosa Spolka v. Fairbairn [1942]; Taylor & Anor v. Caldwell & Anor [1863]), and in the CISG (Article 79).

?2 Prof. Gouveia examined the available information on the arbitral proceedings between Archirodon v. General Company for Ports of Iraq (2019) and Gasum v. Gazprom (2022), as well as the decisions issued in Portugal by the Court of Appeal of Lisbon (Proc. No. 19222/20.1T8LSB.L1-6 [2021]) and by the Court of Appeal of Guimarães (Proc. No. 3409/21.2T8BRG.G1 [2022]).

?3 As Prof. Brunner pointed out, on the one hand, Article 6.2.3 of the UPICC provides for the duty to renegotiate, while the CISG Advisory Council understands there is no such duty under the Convention. In national legal systems, opinions are equally divided; the duty to renegotiate is generally not accepted in civil law systems and is underdeveloped in common law systems – despite some scattered express rules (*e.g.*, in France) and interpretations based on the general principle of good faith (*e.g.*, Italy).

?4 The cases highlighted by Prof. Bruner, which entailed court-ordered renegotiations following an interim decision, are Florida Power v. Westinghouse (1984) and Gasum v. Gazprom (2022).

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