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Arbitration With Public Entities in Brazil: Must Regulatory Agencies Participate?

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On 16 June 2023, the Brazilian Superior Court of Justice (“STJ”) resolved the Appeal in Special Appeal n. 1,905,505/SP (“[Appeal](#)”), reported by Justice Francisco Falcão. The decision was appealed, so that the case will still be judged by the STJ’s second chamber. Nonetheless, the decision is a relevant development concerning arbitration with public entities in Brazil, which has been a hot topic of domestic arbitration in the country for decades. The STJ decision ruled not only on the possibility – and necessity – of a regulatory agency participating in arbitration proceedings between a concessionary and the relevant state entity but also on the limits of extending the effects of an arbitral award over a non-participating third party.

Background

The Appeal was filed by SANESSOL, a company that was awarded a public bid for the provision of sanitation services in the City of Mirassol by the Municipality of the city in 2007. In 2012, SANESSOL requested a tariff revision, arguing for the necessity of re-establishing the contractual balance. Pursuant to Municipal Decree No. 3,066/2007, the matter was evaluated by the Mirassol Water and Sewage Services Regulatory Agency (“ARSAE”), which denied the request in the administrative sphere.

Subsequently, SANESSOL and the Municipality negotiated an amendment to the concession contract (“Contract”), agreeing upon a provisory adjustment and determining that the permanent tariff revision would be discussed by means of arbitration proceedings to be filed in accordance with the arbitration agreement contained in the Public Tender Notice (“Notice”). SANESSOL and the Municipality jointly filed for arbitration before the Chamber of Conciliation Mediation and Arbitration CIESP/FIESP (“CAM CIESP/FIESP”). Former STJ Justice Prof. Massami Uyeda was nominated as the sole arbitrator by the President of CAM CIESP/FIESP. In January 2017, the sole arbitrator granted SANESSOL’s requests (“Award”).

Although the case involves several interesting discussions on arbitration involving public entities, the Appeal deals specifically with the ARSAE’s participation in the arbitration, which, albeit requested by the Municipality, was opposed by SANESSOL and rejected by the sole arbitrator, who stated that the ARSAE was not a part of the bidding process or of the Contract and, consequently, should not be a party to the arbitration.

Despite the Award, the ARSAE published Ordinance No. 2 in March 2017 (“Ordinance”) (i) prohibiting any tariff revisions; as well as (ii) expressly mentioning that the ARSAE (ii.a) was not a party to the arbitration; and (ii.b) would be the only competent authority to rule on the matter. SANESSOL then filed a motion for annulment of the Ordinance, which was denied both by the lower instance court in Mirassol and by the São Paulo State Court (“TJSP”). When judging the Appeal, the reporting Justice at STJ reverted TJSP’s decision, granting SANESSOL’s motion.

Analysis

The decision rendered by the STJ reinforces the use of arbitration as a valid dispute resolution mechanism in Brazil, even when involving public entities. This, however, is not the most interesting aspect of the discussion, as the revision of the [Brazilian Arbitration Act](#) in 2015 buried most discussions in that regard and both the Contract and the Notice contained clear arbitration agreements. The main aspect of the discussion is, thus, the possibility and necessity of the relevant regulatory agency participating in arbitration that involves a subject that, in the administrative realm, would be under its jurisdiction.

When ruling the Appeal, Justice Francisco Falcão highlighted that not only the Contract allows for arbitration, but that the ARSAE approved the amendment by means of which SANESSOL and the Municipality agreed that the tariff revision would be subject to arbitration. Consequently, the publication of the Ordinance would violate the principle of legal certainty.

The STJ’s approach to the discussion is very interesting, as Justice Falcão – differently from the sole arbitrator – was not asked to evaluate whether the ARSAE could be a party in the arbitration, which is a procedural discussion, but rather whether it was mandatory for the agency to participate in arbitration proceedings, as per the relevant administrative laws. Justice Falcão then correctly applied the relevant principles of public law, especially when finding that the Ordinance was illegitimate, as the ARSAE approved the submission of the dispute to arbitration and was, thus, acting contradictory with its own behavior.

This is a particularly relevant aspect of the dispute that appears to have been neglected by the lower instance courts. Not only was the arbitrator correct in denying the ARSAE’s participation in the arbitration, but the ARSAE should also be considered unable to argue the invalidity of the Award from a public law perspective, as it expressly agreed with the matter being subject to arbitration, exercising its authority.

An aspect that was not evaluated by the STJ, but was discussed throughout the dispute, is whether ARSAE’s regulatory competence would extend to the matters of rebalancing the Contract – as such readjustment would demand reviewing the tariffs, which, pursuant to the relevant laws, would be under ARSAE’s jurisdiction. It appears, however, that this argument would also not justify the maintenance of the Ordinance, as this discussion would be superseded by the Award, which was validly rendered and was not challenged.

It is interesting to note that the dispute did not arise as an action for the annulment of the arbitral award – which, as far as the public records show, was never filed by the Municipality – but as an attempt by the winning party to make the Award effective.

Conclusion


The discussion in the Appeal is of particular interest to those working with regulated sectors in Brazil, as it may become a relevant precedent for the discussion on participation of regulatory agencies in arbitration. The Brazilian arbitration market will definitely follow closely the next decisions to be issued by the STJ Chamber and the STF on this case.

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