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Reforming the Paraguayan Arbitration Act: The Good, the Bad, and the Ugly

Raul Pereira de Souza Fleury (FERRERE Abogados) · Monday, May 19th, 2025

On March 18, 2025, the Office of the Paraguayan Presidency's Legal Counsel submitted to the Paraguayan Arbitration and Mediation Center (the "Center") its draft to modernize Law No. 1879/2002, the Paraguayan Arbitration Act (the "Project"), following a recent trend in other jurisdictions amending their arbitration legislation (e.g., France, the UK, and Germany). The Center has invited public comments from practitioners and stakeholders.

Enacted over 20 years ago, the Paraguayan Arbitration Act is based, almost entirely, on the UNCITRAL Model Law on International Commercial Arbitration (the "Model Law"). Its provisions are further reinforced by Paraguay's accession to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention").

The Project proposes to amend 19 articles and introduce 12 new ones, addressing key issues such as the form of arbitration agreements, non-signatories, the ordinary court's obligation to compel arbitration, interim measures, and the procedures for annulment and recognition and enforcement of domestic and foreign awards.

Rather than providing an exhaustive review of the Project's proposals, this post highlights what can be classified as "the good, the bad, and the ugly" (pun intended). While the drafters assert that the Project's purpose is to align Paraguayan arbitration practice with international standards, some proposed amendments may have the opposite effect.

The Good – The Court's duty to compel arbitration

Article 11 of the Paraguayan Arbitration Act contains the well-established rule that courts must refer to arbitration disputes subject to an arbitration agreement "unless it finds that the agreement is null and void, inoperative or incapable of being performed."

The Project strengthens this rule by introducing a higher threshold: courts may only retain jurisdiction if it is satisfied that the arbitration agreement is "clear and manifestly null, ineffective or incapable of being performed."

This is a welcome improvement. It endorses the negative effect of the *Competence-Competence* principle, as developed by the late Prof. Emmanuel Gaillard and Dr. Yas Banifatemi, under which

arbitrators have priority (though not exclusivity) in ruling on their own jurisdiction.[1)]

Although Paraguayan courts have previously acknowledged this principle, they often did so superficially, merely including citations of academic works without fully applying the standard. In one case, for example, a court stated that arbitral tribunals have jurisdiction "when the parties have brought their dispute directly before it; however, if the matter is brought first before the courts, the court seized may also decide, in the first instance, on the existence and validity of the arbitration agreement"[2)] thereby undermining the very effectiveness of arbitration clauses.

The proposed amendment aims to correct this problem by adopting a standard of review already recognized in other Model Law jurisdictions.[3)] In a jurisdiction with limited judicial specialization in arbitration, the new wording would guide courts to perform only a *prima facie* review of arbitration agreements before referring disputes to arbitration.

The Bad – Extension of Arbitration Agreements to Non-signatories

Many of the Project's proposals fall into this category, but one in particular deserves attention: the amendment to article 10 of the Paraguayan Arbitration Act regarding an arbitration agreement's formal requirements.

The new article 10 *bis* seeks to regulate the extension of arbitration agreements to non-signatories, recognizing only two scenarios: (i) when a party's consent to arbitration can be inferred from active participation in the negotiation, execution, performance and/or termination of the underlying agreement (a nod to *Dow Chemical*); and (ii) when the non-signatory intended to benefit from the underlying agreement (third-party beneficiary doctrine).

While some guidance is useful, codifying only those two cases risks limiting the development of the law in this respect. Comparative case law recognizes multiple other bases for binding non-signatories, such as assignment, agency, piercing of the corporate/alter ego, estoppel, and incorporation by reference among others. [4)]

Virtually no national arbitration legislation and international arbitration conventions regulate this issue, and with good reason. As Gary Born points out, the few national laws that have attempted to legislate this matter have provided "limited textual guidance, and their terms have been subject to inconsistent judicial treatment." [5)]

The better approach is to allow courts and arbitral tribunals to assess each case individually, considering the facts surrounding the parties' intent and the extent to which and the circumstances under which non-signatories subsequently became involved in the performance of the agreement and in the dispute arising from it. [6)] Overregulation in this area could stifle necessary flexibility and risk rigid, inequitable outcomes.

The Ugly – Recognition and Enforcement / Annulment

Despite the strong foundations of the Paraguayan arbitration legislation, the Project introduces significant–and troubling–changes to the rules on the recognition and enforcement, and annulment of arbitral awards.

- **Recognition and Enforcement**

The Paraguayan Arbitration Act is a dualist arbitration legislation, meaning that it regulates both domestic and international arbitration within the same framework. In this context, articles 44 and 45 govern the recognition and enforcement of "all arbitral awards", expressly incorporating international conventions like the New York Convention.

The Project proposes amending article 44 to create distinct regimes for domestic and foreign arbitral awards. Under the amendment, national awards (i.e., those rendered in arbitrations seated in Paraguay) would bypass the recognition phase and proceed, directly, to enforcement. Challenges would be limited to three defenses under article 526 of the Paraguayan Code of Civil Procedure ("CPC"): falsehood of the award, lapse of the 10-year statute of limitations, and total or partial payment of the award.

This proposed change is deeply concerning. It departs from established international standards, such as the ones envisaged in the New York Convention and the Model Law, which recognize the right to challenge the validity of awards at the recognition stage—"irrespective of the country in which it was made". [7)]

Importantly, the challenges provided for in the recognition process deal with significant defects in the arbitral process, such as the validity of the arbitration clause, the arbitrability of the dispute, or due process violations. The simple fact that the award was rendered within the Paraguayan jurisdiction does not mean that these defects may not occur. Removing this procedural safeguard denies the enforced party an essential defense mechanism and undermines the legitimacy of arbitral outcomes.

- **Annulment**

Even more problematic is the proposed new article 40 *bis*, which would allow parties to agree that arbitral awards be subject to appeal on the merits. This amendment runs contrary to the basic premise that arbitration offers final and binding decision, free from a subsequent judicial review on the merits. Finality is one of the key reasons sophisticated commercial parties choose over court litigation. Reintroducing appeals on the merits would not only discourage arbitration in Paraguay but also revive an outdated model from the 20th century, when arbitral awards could be appealed under the CPC.

In recent decades, the global trend—reflected in the Model Law and the New York Convention–has been toward a limited, exhaustive set of annulment grounds. Parties entering into arbitration agreements expect quick and final resolutions, not protracted litigation over the substance of arbitral decisions. [8)]

If parties seek recourse to appeal, they should opt for litigation, not arbitration.

Conclusion

The Project to reform the Paraguayan Arbitration Act contains both promising and troubling proposals. Strengthening the *Competence-Competence* principle is a welcome step toward harmonization with international best practices. However, the over-regulation of non-signatory issues and the dismantling of core protections in award enforcement and annulment would certainly undermine the credibility and attractiveness of Paraguay as an arbitration seat.

Likewise, the Project includes many other provisions worth examining. Some, such as the regulation of disputes among heirs and estate executors, are promising. Others, like the provisions on arbitrators' responsibilities and fees reimbursements, raise further concerns. As Paraguay moves forward with reform, it must ensure that modernization efforts do not erode the very features that make arbitration a preferred dispute resolution mechanism for international commerce.

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References

?1 Yas Banifatemi and Emanuel Gaillard, *Negative effect of Competence-Competence: The rule of priority in favour of the arbitrators*, in E. Gaillard & D. Di Pietro (eds.), Enforcement of Arbitration Agreements and International Arbitral Awards: The New York Convention in Practice (Cameron May, 2008) 257.

?2 *EDUCPA v. Rosario del Pilar López*, Decision No. 150 dated April 7, 2014, Court of Appeal of Asunción, Third Chamber.

?3 See, e.g., Article 485(VII) of the Brazilian Code of Civil Procedure, which expressly establishes that the State judge must extinguish the court proceedings, without making any decision on the merits, if: (i) one of the parties argues the existence of an arbitration agreement; or (ii) the arbitral tribunal has already recognized its competence; Article 17 of the Panamanian Arbitration Act states that courts must dismiss *in limine* claims subject to an arbitration agreement; *Astivenca Astilleros de Venezuela, C.A. v. Oceanlink Offshore A.S.*, Supreme Court of Justice of Venezuela, Exp. No. 09-0573, November 3, 2010.

?4 *Thomson-CSF, SA* v. Am. Arb. Ass'n, 64 F.3d 773, 776 (2d Cir. 1995); *Dallah Real Estate & Tourism Holding Co. v. Ministry of Religious Affairs, Pakistan* [2010] UKSC 46, ¶106 (U.K. S.Ct.); *ICC Case No. 6268*, Final Award, ICC International Court of Arbitration Bulletin Vol. 1, No. 2 (1990); Gary Born, *International Commercial Arbitration* (Kluwer Arbitration Law, 2021) 1531 – 1599.

?5 Gary Born, International Commercial Arbitration (Kluwer Arbitration Law, 2021) 1524.

?6 *ICC Case No. 9517*, Interim Award, ICC International Court of Arbitration Bulletin Vol. 13, No. 2 (2002).

?7 Model Law, article 35(1).

?8 Gary Born, International Arbitration: Law and Practice (Kluwer Law International, 2016) 394.