Arbitration in government contracts in Brazil

Back to Arbitration Committee publications (/LPD/Dispute_Resolution_Section/Arbitration/Publications.aspx)

Thiago Marçal
Managing Partner, Almeida & Marçal Advogados, Sao Paulo, Brazil
thiago@almeidaemarcal.com.br (http://thiago@almeidaemarcal.com.br)

Liliana de Almeida Marçal
Senior Partner, Almeida & Marçal Advogados, Sao Paulo, Brazil
liliana@almeidaemarcal.com.br (mailto:liliana@almeidaemarcal.com.br)

Arbitration is regulated in Brazil by means of Federal Law No 9,307, which in its original version did not expressly state the possibility of the Public Administration to elect this mechanism of dispute resolution in its contracts. This omission generated intense doctrinal and jurisprudential debates on the legality of the insertion of arbitration clauses in those contracts

In view of such omission, the Federal Court of Auditors issued decisions pointing out the illegality of a contractual clause that elected arbitration as a means of resolving conflicts involving the Federal Union, arguing, in summary, that: (1) the arbitration procedure is confidential, which does not meet the publicity required for administrative contracts, as determined by article 37 of the Brazilian Constitution and article 3 of Federal Law 8.666/93 – General Bidding Law; and (2) the public interest is a non-disposable right – in administrative contracts, there is the supremacy of the public interest that cannot be appropriated by anyone (Judgments by the Brazilian Supreme Court nos 583/2003, 584/2003 and 631/2003).

Moreover, analysing the legislation on Public Service Concessions, specifically article 23-A of Federal Law No 8,987/95, which provides for the possibility of adopting private mechanisms to resolve conflicts arising from the concession contract, the Federal Court of Accounts restricted its scope by determining that it should be sought to classify this contractual clause as a way of providing both the Public Administration and third parties with the possibility of contracting, by mutual agreement, technical opinions from specialists on the subject, providing better conditions for discernment for the parties, without, however, giving these opinions the character of a final sentence not subject to appeal or ratification by the Judiciary, as provided for in the Arbitration Law.

In the same line, the classical doctrine did not allow arbitration to resolve conflicts in contracts entered into by the Public Administration, as it understood that there would be a violation of the constitutional principles of legality, non-voidability of the Judiciary and non-disposable rights of the public interest.

However, long before the enactment of the Arbitration Law and in force of the 1967 Constitution, the Brazilian Supreme Court, in the 1973 judgment of Extraordinary Appeal 71467 ('the *Lage* case') recognised the legality of the Federal Union to submit to the arbitration solution, to settle the question of determining the indemnity value due to the incorporation into the national heritage of assets owned by the Lage Organization declared of interest to the economy and national defence, in a period of the state of war – Decree Law Nos 4648/1942 and 9521/46. After agreeing with the determination of the indemnity value by arbitration award and requesting the opening of special credit, the Federal Union changed its understanding, refusing to accept the arbitration sentence, forcing the said Organization to use the

Judiciary that recognised the validity of the arbitral commitment signed, for the following reasons: (1) the national system has always admitted arbitration as an alternative form of conflict resolution; and (2) the contractual autonomy of the state which, in the *Lage* case, did not act as a Public Power.

Modern jurists, following the position of the Brazilian Supreme Court, began to argue that Public Administration could choose to resolve its disputes in the arbitration court, in the hypotheses of disposable rights, clarifying that the Brazilian Arbitration Law, did not impose any restriction on the Administration, by providing in article 1 that all persons capable of contracting may use arbitration to resolve disputes. Furthermore, the Brazilian Bidding Law, which regulates administrative contracts, determines that the principles of general contract theory and private law provisions (article 54) apply to those, which include arbitration. It should be added that Law No 8,987/95, which deals with the public service concession and permission regime, stipulates that among the essential clauses of the concession contract is the one that provides for resolving contractual differences amicably (23, XV). Finally, Law 11.079/04, which provides for the general rules for bidding and contracting public-private partnerships within the scope of the Public Administration, allows the use of arbitration in conflicts arising from contracts entered into by the Public Administration, provided that the proceeding takes place in Brazil and in Portuguese (article 11, III).

At the same time, several international entities and bodies that signed contracts and agreements with the Federal Union, states and municipalities, began to demand the provision of arbitration in the contracts to be signed, which rekindled the doctrinal debate. Still, private national investors are interested in concluding administrative contracts for the execution of works and services; they preferred the speed of the arbitration procedure and the specialisation of the arbitral awards to settle disputes with public entities, avoiding the well-known burden and slowness of the Brazilian Judiciary. In this context, the State of Minas Gerais enacted Law No 19,477/2011, which authorises the adoption of the arbitration award in contracts signed with that entity of the federation. In the same vein, several public-private partnership contracts signed by the State of São Paulo and the Municipality of Rio de Janeiro adopted arbitration as a method of dispute resolution.

In order to consolidate the practices already adopted by Brazilian states and municipalities, as well as to eliminate the legal uncertainty regarding the legality of the use of arbitration in government contracts, a draft law to revise the Arbitration Law was presented (PL nº 406/13), which subsequently became Federal Law No 13,129/2015, which added paragraph 1, to article 1, expressly authorising the Public Administration to use arbitration in contracts involving disposable rights.

Subsequently, Brazilian states and municipalities edited normative texts, regulating internal procedures for registering arbitral chambers, selection of independent and impartial arbitrators, as well as publicising the acts, providing greater security and guarantee in the use of arbitration by the Public Administration. Decree nº 64.356/2019 of the State of São Paulo and the recent Law nº 17.324/2020, of the Municipality of São Paulo, stand out, the latter instituted a public policy to avoid the judicialisation of conflicts and provided for the use of arbitration to settle disputes involving disposable rights.

Thus, the presence of the Public Administration in arbitration implies specificities in the procedure, provided for in article 3, paragraph 3 of the Arbitration Law, which must be strictly obeyed: (1) publicity of acts: there was an express legal determination for the transparency of acts to allow social control, which ranges from justifying the public interest by adopting arbitration, including proving that it is a disposable right. Until the final arbitration decision, the arbitral tribunal is responsible for ensuring the required publication of its award; (2) strict legality of the acts: arbitration will always be legal, which excludes the application of equity, that is, the arbitrators will not be able to use their personal values, that is, subjective criteria for analysing the facts and evidence, but only legal criteria defined by law; (3) definition of the arbitral chamber: depends on its specialisation in public law matters and prior registration or collaboration agreement with the Public Administration; and (4) execution of the arbitral award: it is subject to the precatory system provided for in article 100 of the Federal Constitution.

In many other countries, the understanding prevails that disputes involving the Public Administration can be resolved by arbitration. American courts, in turn, have recognised that litigation with both the federal and state government as parties is subject to resolution by Alternative Dispute Resolution (ADR). In that country, the Administrative Conference, a federal agency that does research on the procedures of federal agencies and monitors them, has been at the forefront of this trend, in the sense of increased use of ADR methods for dispute resolution, in which a government agency is a part.

The provision for the use of arbitration in contracts does not violate the right to file a lawsuit in court, according to the decision of the Brazilian Supreme Court, which concluded that such principle could not prevent the parties' option to opt for the extrajudicial resolution of conflicts, recognising the constitutionality of the Brazilian Arbitration Law incidentally.

In other words, the national legislation in force allowed the use of arbitration to settle conflicts in an administrative contract in which the state acts without the supremacy of its typical activity which resulted in enormous benefits in the signing of administrative contracts, agreements, and terms of cooperation with international entities, which already used this institute to resolve conflicts, in addition to national contracts providing the necessary legal certainty for the parties.

However, some aspects regarding the costs and expenses of arbitration are still pending the necessary regulation when the Public Administration is present. The federal arbitration law determined that the parties' liability for costs and expenses will be defined in the arbitration award (article 27). In turn, the State of São Paulo Decree established that the expenses would be advanced by the arbitration claimant (article 4, para 1, item 5). This provision stems from the fact that the private sector, in most cases, questions the Public Administration's failure to comply with the contract. Nevertheless, if the Public Administration is the applicant, should it also advance the amounts of the individual's expenses? Does such conduct serve public interest? However, because it is a public budget, the use of which has internal and external control, there would need to be specific regulation, which exists neither in federal law nor in state and municipal rules. The issue of attorney fees also deserves special regulation to avoid the Public Administration having to reimburse stratospheric amounts, for example by previously defining the maximum value to be reimbursed.

The advancement of Brazilian legislation in the regulation of the use of arbitration by the Public Administration, defining the particularities of the arbitration procedure in this hypothesis, did not detract from the nature of the institute, on the contrary, it made it compatible with the legal regime of public law, expanding its application. It is also essential to complement the regulations to cover expenses, costs, and attorneys' fees.

Back to Arbitration Committee publications (/LPD/Dispute_Resolution_Section/Arbitration/Publications.aspx)