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Litigation v. Arbitration in the Americas. Advantages and Disadvantages.

Brazilian View *

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In order to approach the proposed subject matter and make comparisons between the submittal of dispute to court or to arbitration, to evaluate the advantages and disadvantages to adopt one or other way, it is necessary to limit the matter to the scope of the equity rights available, that is, those rights that the legislation permits to be freely disposed of by the parties. In this regard, matters related to the criminal, tax, family law, etc. are excluded. All disputes arising from rights freely agreed to within the scope of general obligation law (contracts) may be submitted to arbitration.

1. – Arbitration

The subject matter of this lecture, from the Brazilian point of view, if proposed before the new law on arbitration, Law No. 9307, of September 23, 1996, would certainly tend against arbitration before state justice. Accordingly, the matter was set forth in the Code of Civil Procedure, so as to discourage its use, for two reasons: first, it did not grant binding effect to the arbitration clause which, if not complied with, would have the same effect of default as any contractual clause; it was considered to be a simple promise to contract. The arbitration would only be constituted and obligatory if the parties executed later the arbitration agreement. Second, the issued arbitration award, in order to

be effective and valid, required prior judicial ratification. In view of these circumstances, the arbitration was very little used within the domestic scope, and in international arbitration the situation was a little better, since Protocol of Geneva of 1923 is in force in Brazil, for the recognition of arbitration clauses (Decree No. 21187/32), setting forth that in international agreements the arbitration clause had binding effect. This understanding was ratified by the Higher Courts case law (Special Appeal 616 – RJ – 890009853-5, j. 09.24.90 – Lex Case law of STF/TRF, Feb., 1991, 18:108-30).

With the arbitration law of 1996, the situation was changed and arbitration started to count on more effective instruments that enabled its use. The law of arbitration is originated from the Model Law on International Commercial Arbitration of the United Nations Commission for International Business Law Development – UNCITRAL, of 1985 and widely privileges the principle of autonomy of will.

Below we will underline the mains characteristics of the Brazilian arbitration statute, for, then, to approach some polemic aspects and the understanding of Judicial Courts, that in this small period of effectiveness (almost 5 years), contributed a lot to dissipate mistakes and misunderstandings as to the correct interpretation of the law, as well as has been demonstrating that the Brazilian Judiciary privileges the institute, both in lower courts and in the highest Justice Court, the Supreme Federal Court – STF, specially in the matter involving the constitutionality of some provisions of law, approached in the course of this exposition.

1.2 Characteristics of the Arbitration Law

1.) The stipulation of arbitration will take place through an **arbitration agreement** (**"convenção de arbitragem"**), that include both the **arbitration clause** ("**cláusula compromissória"**) and the **compromise** ("**compromisso arbitral"**). Art. 3 of Law No. 9307/96 sets forth as follows: *"the interested parties may submit the solution of disputes to the arbitration tribunal upon arbitration agreement, which is understood as the arbitration clause and the compromise."*

The **arbitration clause** ("cláusula compromissoria") is the convention through which the parties in one agreement undertake to submit to arbitration the disputes that may arise, as to such agreement. It must be set forth in writing, and may be inserted in the agreement itself or in a separate document referring to it (art. 4th and 1st §). In turn, the **compromise** ("compromisso arbitral") is the convention through which the parties submit a dispute to arbitration of one or more people, which may be in or out of court. (art. 9th). This document will describe the dispute to be settled, name and qualification of the arbitrators and their alternatives, the procedural rules, the authorization for the arbitrators to decide by equity, that is, out of legal rules, according to its fairness criterion, according to their real knowledge and understanding, finally, the provisions of article 10 must be complied with. We will be back to these questions elsewhere, when analyzing the act of setting the arbitration.

2.) The law permits the **application of uses and customs and the international rules of commerce**, and the parties may agree that the arbitration is performed based on the general law principles, on the uses and customs and in the international rules of commerce (art. 2, 2nd §). It is the effective acknowledgment of the rules established by the international community that make easier and know all commercial

mechanisms, such as Incoterms and the Uniform Customs and Practice for Documentary Credits. In addition, it protects *Lex Mercatoria* which has in arbitration practice its the most authentic application.

3.) Law provides for a specific procedure to comply with the arbitration clause, that has obligatory nature and binding effect, requiring the parties to institute the arbitration. One of the main characteristics of the convention of arbitration is to put away the competence of the state jurisdiction. Thus, if there is a arbitration clause and resistance to the institution of arbitration, the interested party may file a lawsuit to institute the arbitration. (art. 7).

4.) The parties may freely choose the rules of the material law that will be applied in the arbitration, provided that there is no violation of the good practices and the public order (art. 2, 1st §). The procedural rules, when not set by the parties, will be provided by the arbitrators, when it is not an arbitration administered by an Institution of Arbitration that as its own regulation. It must be noted that in the choice of foreign law to regulate the material right to interpretation will take place according to the practice of the doctrine and case law of such country.

5.) The arbitration award has the same effects as the court judgment, and is not subject to certification or appeal (arts. 18 and 31).

6.) The law established the **competence-competence** principle, that is, the arbitrator is competent to decide on his/her own competence (arts. 8, sole § and 20). In this regard, the new law follows the more modern arbitration legislation, of which the Spanish law 36/88, the case law and French law and the Standard UNCITRAL Model Law are

underlined. As well as the judge, the arbitrator has competence to decide on his/her own competence as to the arbitration level.

7.) The law provides for the principle of the autonomy of the arbitration clause, and the validity an agreement may be contested and this doubt must be settled by arbitration, since the arbitration clause is independent from the agreement and the allegation of nullity does not affect it (art. 8).

8.) In case, during the arbitration, the parties reach a friendly agreement as to the dispute, the arbitration or arbitration court may declare such fact by an arbitration award (art. 28).

9.) The law provides for the arbitrator's ethic code, that in the performance of their function they must proceed with impartiality, independence, competence, and diligence and discretion (art. 16, 6th §). It is worth noting that any capable person entrusted by the parties may be an arbitrator (art. 13). Brazilian law does not impose any restriction as to the nationality of the arbitrator.

10.) The Law enables the rectification of the arbitration award, when there is material error, obscurity, doubt or contradiction in the arbitration award. The parties may request clarifications and rectification of the arbitration award (art. 30).

11.) The access to the judiciary is provided as action of determination of nullity of the arbitration award upon the existence of the defects set forth in art. 32 (art. 33) action for enforcement of the arbitration award (art. 31) and action for "embargos" of the debtor (art. 33, 3rd §). The determination of interim measures will be up to the arbitrators during

the arbitration, however its coercive execution will require a request to the competent judge, as set forth in art. 22, paragraph 4 of Law. It must be noted that the need to request an interim measure before the judiciary and prior to the institution of the arbitration does not represent waiver to the arbitration nor prevents that after the determination of the preliminary order the matter is referred to the arbitrators, who may even revoke it (see Carlos S. Lobo and Rafael Rangel Ney "Revogação de medida liminar judicial pelo juízo arbitral", Revista de Direito Bancário, do Mercado de Capitais e da Arbitragem, no. 12, Apr/Jun 2001, p. 357/64).

12.) The law privileges and expressly acknowledges the institutional arbitration together with *ad hoc* (arts. 5 and 21). Arbitration Chambers and Centers operate in several location, such as those existing in São Paulo and that are frequently appointed to settle national and international disputes: Câmara de Mediação e Arbitragem de São Paulo do Centro and Federação das Indústrias do Estado de São Paulo CIESP/FIESP (cmarbitragem@fiesp.org.br) and Centro de Arbitragem da Câmara de Comércio Brasil-Canadá (centroccbc@ig.com.br).

13.) Law regulates in chapter VI the recognition and enforcement of foreign arbitration award, pointing out that it will be acknowledged and enforced in Brazil according to the international treaties with effectiveness in the internal order and, in its absence, according to this law. Therefore, it privileges the international treaties, as in this case, in view of the commitments undertaken by Brazil in the nations convention. The International Treaty is the first source of the Public International Law, as set forth in article 38, letter "a" of the Statute of the International Court of Justice (The Hague). However, considering that Brazil up to this moment did not ratify the Convention of New York

of 1958, on the Recognition and Enforcement of Foreign Arbitration Awards, the arbitration law introduced in the internal legal system the provisions of this Convention, and it must be underlined the principles of single certification and the inversion of the burden of proof. Based on these provisions, STF has been ratifying foreign arbitration awards, even if issued before the effectiveness of the Brazilian arbitration law, which as it is adjective law apply to the ongoing actions (see. Contested Foreign Judgment 5.378-1 French Republic – STF – j. 02.03.2000-Justice Maurício Corrêa – DJU 02.25.2000, Revista de Direito Bancário, do Mercado de Capitais e da Arbitragem, n. 8, Apr./Jun., 2000 p. 391/94).

14.) As regards the international conventions with internal effectiveness, it is important to notice that Brazil has ratified the Interamerican Convention on International Commercial Arbitration done at City of Panama of 1975 (Decree No. 1902 of 05.09.96). This convention is effective in all countries of MERCOSUR and 16 American countries adopt it. In general lines, this Convention sets forth: a) the recognition of the arbitration clause with obligatory nature and binding effect, whether through clause inserted in agreement or through exchange of letters or communications by telex; b) the non-necessity of dual ratification of the arbitration award; c) the inversion of the burden of proof; d) the application of the regulation of arbitration of the Interamerican Commercial Arbitration Commission – CIAC. It must be noted that Interamerican Convention on Extraterritorial Effectiveness of Foreign Arbitration Judgments and Awards is also in force in Brazil, done at Montevideo in 1979, in force in all countries of Mercosur (Decree No. 2411, of 12.02.97). It applies to judicial judgments, arbitration awards and foreign jurisdictional decisions in civil, business and labor areas. The provisions thereof are eminently procedural. This Convention

has an interesting peculiarity. It underlines that it has application supplementary to the Convention of Panama of 1975, as regards the foreign arbitration awards, that is, a matter not regulated in the Convention of Panama, but provided for in that of Montevideo, completes it and incorporates thereto. It must, further, be noted that, within the scope of MERCOSUR, the International Convention on Private Commercial Arbitration was done in Buenos Aires, in 1998, and was approved by the Brazilian Parliament, but needs a decree of promulgation to be issued by the President of the Republic.

15. We have also noted that dispute settlement by arbitration reached partnerships of the State with the private sector, in particular public utility concessions, in the so-called financial clauses. In turn, the regulatory clauses, are excluded from being submitted to arbitration ("ius imperium"). The legal starting landmark was Law No. 8987, of 02.13.95, art. 23, item XV, that determined to be essential clauses in concession agreements those related to forum and the way of contractual dispute settlement, widening and clarifying the provisions of the bidding law (Law No. 8666/93, art. 54). The possibility to use the arbitration was ratified by the judiciary, according to the decision issued by the Court of Justice of the Federal District in the Writ of Mandamus No. 1998002003066-9, 05.18.99, when stating that "... by art. 54, of Law No. 8666/93, the administrative agreements are governed by their clauses and public law provisions, and private law principles are applied to them in a supplementary way, which reinforces the possibility of adoption of the arbitration procedure to settle any contractual disputes...". Thus, from the master line drawn by Law No. 8987/95, several laws succeeded and were enhancing the application of the institute of arbitration. Within the scope of the concession agreements executed by the National Telecommunications Agency – ANATEL, Law

No. 9472/97 determines, in art. 93, XV that these agreements will provide on the forum and out-of-court way of contractual dispute settlement. In concession agreements executed by the National Petroleum Agency – ANP, Law No. 9478/97, art. 43, X, regulates the provision of settlement of disputes related to the agreement and its execution, including conciliation and international arbitration. Recent Law No. 10.233, of June 05, 2001, in art. 35, item XVI, establishes that in concession agreements for waterway transportation there must be a clause providing for disputes related to the agreement and its execution, establishing conciliation and arbitration (see our article "Arbitragem na Concessão de Serviço Público - Perspectivas, Anais do Seminário Jurídico sobre Concessões de Serviços Públicos, Foz do Iguaçu, 06.08.01 – Escola Nacional de Magistratura e Academia Internacional de Direito e Economia).

1.3 The Polemic around Article 7 of Arbitration Law - The Constitutionality acknowledged by STF

The issue of unconstitutionality of the legal institute of arbitration is, fortunately, already overcome. STF, in several instances, including in the judgment of the incident of unconstitutionality commented on below, it ratified the understanding that those under the jurisdiction may waive to the submittal of disputes to the judiciary, as well as they make transactions and waive to rights. The arbitration does not infringe art. 5, item XXXV of the Federal Constitution, "the law will not exclude from the consideration of the Judiciary any lesion or threaten to any right". Said provision, as widely known, is directed to the legislator to prevent laws from instituting parallel courts, suppressing the rights of citizens to resort to the judiciary, in view of the practice adopted in the dictatorship of Getúlio Vargas. The constitutional legislator of 1946, traumatized with

the experience of that time, raised to the constitutional level the prohibition of a legislative initiative that puts away the rights of citizens to resort to the judiciary.

In the unconstitutionality incident in the Regimental Bill of Review in Foreign Judgment no. 5206-7, Kingdom of Spain (that treated the recognition of foreign arbitration judgment accepting the immediate application of the new law, dispensing the dual ratification of the foreign arbitration award) the unconstitutionality of some articles of the arbitration law (arts. 6, sole§, 7th 41st and 42nd paragraph). We will only focus on Art. 7, since the other ones treat the operating reflexes thereof. Art. 7 represents one of the most important innovations of law (in line with the most modern arbitration legislation), providing on the judicial action to institute the arbitration, giving effect to the arbitration clause inserted into contract when there is resistance of the other party to start the arbitration. Justice Sepúlveda Pertence reminded that art. 7, when accepting the arbitration clause would characterize a generic waiver, of a indefinite object, the assurance of access to the jurisdiction. The waiver to the right of action does not exist "in abstracto". During the judgment, Justice Nelson Jobim contested with the argument that the Constitution does not prohibit the parties from agreeing to extrajudicial forms of settlement of disputes that may arise within the scope of a certain agreement, there being, there, no abstract waiver to jurisdiction, but the acknowledgment of the individual freedom. He asserts that, in the action of art. 7 it is the plaintiff, and not the judge, to establish the limits of the conflict that will be subject of the compromise. The judge limits to check whether they are included within the limits of the contract.

Art. 7 of law grants positive effectiveness to the arbitration clause, in view of the resistance of a party to institute the arbitration it freely agreed to. It establishes a legal procedure for the compliance with the obligation to do, to obtain the expected result, in the line of movements to renew the effectiveness of the civil procedure, that prioritize the teleological process, reverting the axiom that every obligation to do not complied with would imply losses and damage. We observe that the arbitration clause does not represent an obligation to commit, since the parties are committed from the moment they executed the agreement and provided for the settlement of disputes by arbitration (binding effect of the arbitration clause). The upcoming obligation is that of instituting the arbitration at the time of the dispute, since, what is expected from such action is the "concreteness" by the judge of the right of the creditor to have the arbitration instituted (see SEC 5 847-1 – STF, the vote of Justice Maurício Corrêa). This is not about replacing the will of the debtor. It does neither refer to the opened and unlimited arbitration clause, but to a business limited within the scope of the agreement.

Justice Ilmar Galvão adds that art. 7, that "the Brazilian judge cannot interpret the new law to make innocuous the provision that equalizes the clause, giving it effectiveness, even if by resorting to the judicial judgment, under penalty of showing to be insensitive to the changes that occurred in the same period in several laws, even because, including, it is in line with the international texts in force in Brazil, such as the Protocol of Geneva of 1923 and the Inter American Convention on Commercial Arbitration done in Panama".

On the other hand Justice Ellen Gracie ponders that "denying the possibility that the commitment value to have full validity and give raise to the specific execution implies to privilege the defaulting party and

denying the submittal to the quick way of dispute settlement, a mechanism for which it freely opted, upon the execution of the agreement where this provision was inserted. It is giving the defaulting party the power of voiding a condition that – given the nature of the involved interests – could have been deemed to be essential for the agreement." In the other votes, Justices Celso de Mello and Marco Aurélio Mello stated the same understanding declaring the constitutionality of Art. 7 and the other ones mentioned.

We note, further, that art. 7 of law give raise to two commands. The first one is that it has a supplementary function, that is, it must be called only in the presence of dry or empty arbitration stipulation, found when the parties to an agreement establish that the future disputes will be settled by arbitration, but set nothing as to the manner of instituting the arbitration or appointment of arbitrators. Thus, when the parties establish the arbitration administered by arbitration institution, having its own regulations and disciplines the way of electing the arbitrators, the application of art. 7 is not proper, and the party wishing to start the arbitration may resort to such institution. The same will occur for "ad hoc" or deferred arbitration procedures (when they remit the election and appointment of the arbitrators to third parties), in which the way of choosing the arbitrators is provided or the way of starting the arbitration procedure is explained. Let us see that, according to the provisions of art. 19, the arbitration will be constituted when this attribution is accepted by the arbitrator. This understanding is supported by the State Courts (Appellate No. 124.217/0, of 09.16.99, TJ-SP) and confirmed by STF, according to the provisions of the judgment reported above. The second one is that art. 7 must be interpreted in its teleological function, noting that its purpose is to institute the arbitration and not, as argued by some people, that would be to make the arbitration agreement.

Finally, after four years of judicial discussion as to the constitutionality of the provisions mentioned in Law No. 9307/96, STF – although the judgment is not yet finished, but defined by absolute majority of votes -, it grants the legal security necessary for the effective use of arbitration in Brazil.

2. – The judicial dispute v. arbitration

Law No. 9.099, of 1995 establishes a distinct procedural for civil matters involving certain demands of up to R$ 6,400.00 (US$ 3000). The parties may appear without attorneys (for disputes of up to R$ 3,200.00 - US$ 1.500), privileges conciliation and transaction and establishes a simplified way for procedure of appeals. Legal entities cannot file actions before the special civil court. It must be noted that the stipulation of arbitration seldom exists for settlement of disputes related to small amounts, which are covered by the special court.

The causes related to arbitration in relations of consumption, have not yet received attention by the authorities and providers of products and services in Brazil, to incentive the settlement of disputes by arbitration, as it occurs in other places (see our article "Arbitragem nas Relações de Consumo no Direito Brasileiro e Comparado", Aspectos Fundamentais da Lei de Arbitragem, Pedro Batista Martins, *et alii*, Rio de Janeiro, Forense, 1999, page 113/41). The matters in this area are either settled in special civil courts or are subject to conciliation in the consumer protection and defense agencies.

In labor disputes, arbitration is being well accepted, considering the results obtained (arbitration awards are issue, in average, in 30 days). In labor justice, only the designation of the first hearing would require almost one year and, for the first level decision, 2 years, in average). The arbitration option is set forth, generally, in labor collective agreements. In São Paulo CAESP - Conselho Arbitral de São Paulo (www.caesp.org.br) operates, which through conventions with employers and workers unions administers labor arbitration procedures. Since its constitution in 1999, CAESP has already issued over 7 thousand (labor and civil) arbitration awards. The amounts involved are of about US$ 1200. It must be observed that many times arbitrators determine, in the arbitration award, the release of the deposits related to Guarantee Fund for Length of Service – FGTS (severance/insurance payment for dismissal without cause) but, sometimes, there is resistance of Federal Savings Bank to comply with the decision of the arbitrator, denying the equivalence of the arbitration award to the judicial judgment ("the arbitrator is a judge in fact and by law, and the judgment he/she issues is not subject to appeal or to the ratification by the Judiciary", is provided for in art. 18 of Law No. 9307/96). In view of the resistance of the bank agent, the interested parties resort to the

Judiciary, filing Writs of Mandamus, that grant the preliminary injunctions requested and confirm them in final judgments. They determined that the bank agent immediately comply with the provisions of the arbitration award (MS No. 2000.61.00.034086-9, 19th Federal Court/SP, 09.06.00; MS No. 2000.61.013042-5, 24th Federal Court/SP, 04.27.00; MS No. 2000.61.00.34087-0, 8th Federal Court/SP, 09.12.00; MS No. 2000.61.00.014218-0, 19th Federal Court/SP, 06.12.00) CAESP has recently had the important participation in the settlement of disputes involving labor liabilities of a financial institution that would be disposed of and needed to be in order.

Civil and business actions of high complexity and amounts are, in Brazil as in any other place in the civilized world, subject to the optimist average of 8 years, for final decision and execution. Many factors contribute to this: the accrual of actions, the proportion of judges/inhabitants, the procedural rules that enable the filing of countless appeals (more than 50); finally, are factors that provide the review of the legislation seeking for alternative disputes resolution, driven by "renewing waves" of the modern civil process, taught by Mauro Cappelletti, when mentioning the three movements started in 1965. "the first ["wave"] turned to the judiciary assistance to the needy, the second focused on the absorption of search for collective legal protection, the third characterized by the internal reform of the procedural technique according to the purposes of the system and in view of the conscience and its *sensitive points*" (*Apud* Cândido Rangel Dinamarco, "Fundamentos do Processo Civil Moderno", São Paulo, 3 ed., Malheiros, vol. I, page 305, 2000).

The arbitration is inserted in these new paradigms of the procedural law, that are universally accepted. The jurisdictional consideration must prioritize the effectiveness and informality (see Recommendation No. R (86) 12, adopted by the Committee of Justices of the Europe Council, when stimulating the use of arbitration as an effective way of access to justice. " Bulletin D'Information sur les Activités Juridiques au sein du Conseil de L'Europe et dans les États Membres", No. 23, Jan./87). In this circumstance, the arbitration jurisdiction must be analyzed as a way of help in the administration of justice. The analysis of cost/benefit relation to adopting one or other way of dispute settlement must be dispensed with. "Justice delay, justice denied", the saying goes. The time factor, the specialty of the arbitrators in the disputed matter, the secrecy that involves the arbitration, the domain that the parties exercise in the arbitration process as the possibility to indicate arbitrators and provide on the procedural rules to be observed by the arbitrator are factors that would tend to favor the arbitration. However, for this, we have also to evaluate other factors that effectively contribute for the success and normal course of arbitration. Among them, to have a legislation that make easier and grants the necessary legal security, a judiciary that discourage the abuses practiced, accepting "pacta sunt servanda' and the principles of good faith and loyalty, that must govern all relations, as well as and, specially, to have arbitration clauses correctly worded, that permit the institution of arbitration, without delays and difficulties.

It is by reminding the teachings of Cândido R. Dinamarco (op.cit. page 318) that we finish up. "It is time to refute conceptualism and conformism. The civil procedure of nowadays is necessarily a civil procedure of results, since without good and effective results, the procedural system does not become legitimate".

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