# ARBITRATION INVOLVING GOVERNMENTAL ENTITIES.

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## 1. Introduction.

Thank you. It's great to be back in Rio. It was here in Rio that we developed the model for the University of San Francisco's externship program, with invaluable guidance and assistance from Anderson Schreiber and Gustavo Tepedino. That externship model has placed our students in law offices all over the world, including India, Rome, Milan, Paris, London, Berlin, Spain, Belgium, the Czech Republic, Copenhagen, Vietnam, China and Mexico City. All these programs had their origin right here in Rio, and so a special thanks to Anderson and Gustavo.

Also, I want to thank Anderson and the Attorney General's office for this invitation to speak on a topic that I've discovered, in developing this talk, has gone unexplored in any of the academic or law practice literature despite its importance – the topic of the distinctive character of governmental arbitration.

Public administration arbitration is especially of interest about Brazil, because Brazil was near last among the major states of the world to adopt arbitration as a means of dispute resolution. Not without historical reason. As those of you familiar with the history know, the caution in accepting arbitration as a principal mode of dispute resolution was both philosophical and political -- rejection of neocolonialism (by way of the so-called Calvo clause that restricted jurisdiction to the state of nationality), and opposition to any potential opening for resurgence of Yankee imperialism.

Brazil, today, presents a very different picture for arbitration. Having legislated the Brazil Arbitration Act in 1996 and the amendments of 2015, having joined the New York Convention on the Enforcement of Foreign Arbitral Awards, and having overcome Constitutional and cultural hurdles of resistance to arbitration, Brazil is now fully engaged in arbitration as a form of dispute resolution for both private parties and government.

Arbitration involving public administration, our concern today, was separately brought into Brazil law by the 2015 amending Act, and has become what is sometimes described as a 'game changer'. The 2015 amendments authorize every public body, including the Brazilian Government as such, to enter into agreements for arbitration of its disputes. This

includes public concession agreements, public-private partnerships and other public entity involvement in the economic life of Brazil, especially its energy and infrastructure sectors. And despite the historical resistance to domination by the legal culture of the Northern hemisphere, Brazil's Arbitration law, in most basic respects, now replicates US and other Western nations arbitration law and the International arbitration law they engendered.

Any risk of Yankee domination of Latin America by way of arbitration is apparently no longer a significant concern, and those of us who have experience in arbitration see that as a healthy development. But don't get me wrong. I certainly am not here speaking as an agent of Trump's 'America First' philosophy. Trumpism is about generating disputes, not resolving them through legal process. And Yankee domination of Latin America is well out of favor among my fellow Californians. Indeed, the present demographics of California are returning us to the Latin family, especially San Francisco, which is well on its way to leaving the United States of Trump.

However, returning to our topic - In light of the new prominence of arbitration for dispute resolution for public administration in Brazil, I would maintain, that what is most important for government lawyers, is perspective – that is, understanding that arbitration brings with it special considerations. This is what I intend to discuss.

But since you are the experts on the law of Brazil, and I am not, I will seek to provide insights that the experience of arbitration in the United States and internationally can provide for your engagement in arbitration in Brazil. I will be drawing mainly on my own experience for a number of decades as an Arbitrator for the American Arbitration Association, experience which has involved US and California governmental entities. I will also be drawing on my study and teaching about international arbitration, as it is in the experience of international arbitration that provides some of the most instructive examples of how arbitration can be best employed for the resolution of disputes involving states and state entities.

For your perspective, for representatives of the state, the analysis should begin with understanding, that the choice to arbitrate is not simply a choice of legal process. It is a strategic choice about what you want to accomplish. The choice to arbitrate, and in what form, is best evaluated for those of you working in the wars of dispute resolution, by weighing the advantages and disadvantages of arbitration in reaching your objectives against alternative strategies for dispute resolution. The alternative strategies range from exercise of power in its most raw form, to the various modalities for utilizing law and lawyers.

Consider the options and their consequences for good government. For example, early in United States labor history, labor disputes were resolved in street fights between iron

club wielding workers and company mercenaries. That was a form of dispute resolution – more or less on the same plane as the dispute resolution process that currently occurs in the form of the drug gang wars of Rio – expression of power its most raw form. For the United States, there evolved, however, the less bloody and more civilized alternative of the legal obligation of 'good faith negotiation', now the core concept of dispute resolution under the US National Labor Relations Act. And now we all have available, both domestically and internationally, a great variety of modalities for nonviolent dispute resolution - negotiation, mediation, litigation, arbitration - and these more virtuous forms of human dispute resolution are now available for virtually every field of law. It is, accordingly, necessary to see arbitration, agreed by way of a contract clause, or *ad hoc* after a dispute has developed, as a political decision, a matter of strategic choice among the available alternatives, as to which you, as government lawyers, need to evaluate the relative costs and benefits.

## II. Advantages and Disadvantages of Arbitration.

What, then, are the advantages and disadvantages? Why would you want arbitrate or not want to arbitrate a dispute in your representation of government or a governmental agency?

You probably have heard the conventional wisdom; that arbitration is cheaper, faster, less encumbered by procedural rules, that it can assure greater confidentiality than litigation, and that now under both international law, and by way of the NY Convention, and in Brazil's domestic law, by way of the Brazil Arbitration Act, an arbitral award is equally enforceable as a court judgment. Actually – arbitration is better as to enforceability -- because the grounds for appeal of an arbitral award are so narrow, both under the New York Convention and most arbitration systems, national and international, and including Brazil's Arbitration law, that arbitration assures greater and generally more expeditious ***finality*** than litigation.

However, like all conventional wisdom, the conventional wisdom about arbitration must be qualified. And the conventional wisdom about arbitration is sometimes just plain wrong. Certainly my experience and study of the reality of arbitration demonstrates the necessity to look deeper than the conventional wisdom.

First, consider the most common proposition of the conventional wisdom about arbitration – that arbitration is faster and more cost effective. It ***is*** usually faster and cheaper, and that may be of considerable significance. One study I've reviewed reports that in 2010,

litigation in Brazil averaged 12 years while the average arbitration took 14 months. So the evidence apparently is that arbitration does normally result in very substantial reduction in time and costs as compared with judicial litigation. It is accordingly particularly more advantageous when time is critical, as for example, for environmental and water rights disputes.

But fully considering the actual experience and record of arbitration, you can see that it is sometimes ***not*** faster nor more cost effective than other modalities of dispute resolution, for any number of reasons. One of the most significant reasons, at least in US arbitration, is that one of the few bases on which an arbitrator's award can be reversed is if the arbitrator has refused to entertain relevant evidence. So the inclination of the arbitrator, interested of course in avoiding reversal of his or her award, is to admit into the proceedings all evidence offered, however tenuous its relationship to the issues. This can extend the time and cost considerably beyond a comparable litigation. Adjudication before a litigation judge is much more constricted by rules limiting the admission of evidence – for example the rule precluding hearsay evidence where a witness would state what he claims to have heard from someone else.

Furthermore, for the arbitrator, the exaggerated admission of evidence is complemented by the reality that the arbitrator is typically paid on an hourly or daily basis. So the arbitrator may be inclined to take any opportunity to run up additional time. The salaried judge, whose salary is the same no matter how heavy or light the caseload is, to the contrary, inclined to do all he or she can to lighten the caseload. So moving a matter to arbitration improves the income for an arbitrator and lightens the caseload for a judge, an attractive result for both. Moreover, as to cost, it is also important to keep in mind, that when you arbitrate, your client is paying the arbitrator by the hour - maybe three of them, depending upon how the arbitration is structured -- along with substantial administrative fees when an arbitral institution is involved, while in judicial litigation, the state pays both for the justice system and the judge.

Another item of conventional wisdom about arbitration being superior to judicial litigation that we need to consider more critically, is that arbitration can better serve to preserve a working relationship between the claimant and respondent, while resolving disputes. This is best illustrated by the standard construction contract of the American Institute of Architects, wherein the architect is in effect designated as arbitrator in being charged to resolve disputes between owner and contractor, so that construction can proceed to completion, notwithstanding the disputes that almost invariably arise before arriving at completion.

My own experience is that once the contractor and owner hire their own lawyers, the relationship between contractor and owner is destroyed, rarely allowing its reconstruction. The project simply stops, irrespective of the availability of architect as arbitrator.

But for governmental arbitration, stopping may not be possible. The need to get along with the various constituencies that government governs, on a continuing basis, is thus one factor that makes arbitration more attractive for government than judicial litigation. This can be true for disputes between government agencies that must continue in a cooperative relationship, for disputes between a government agency and a public/private partnership, or between government and an entity with which the government necessarily has a long term evolving relationship, such as between the government of Brazil and the oil company Petrobras. So the conventional wisdom that arbitration can help sustain an important relationship can be correct, and especially advantageous for government and its agencies.

Also what needs to be addressed, but with greater skepticism, is the conventional wisdom that a principal value of arbitration is that it can better assure confidentiality than other modalities of dispute resolution, particularly as compared with judicial litigation. In commercial litigation, the principle of confidentiality serves to secure such matters as trade secrets and reputation, and avoiding stock impacts. But as a government lawyer should you prefer the confidentiality that arbitration can more likely assure? It is always tempting, of course, to extend a blanket of confidentiality over one's affairs, whether arising in the office or in the bedroom. But the better angels of one's nature, as a government attorney, instruct otherwise. For a government lawyer, confidentiality can be the greatest vice, not virtue. Confidentiality, though touted as private virtue, is a public vice for the government lawyer working in the various arenas of public interest. Publicity and transparency are essential virtues of good government, not to be avoided, but to be cherished for democracy to work as it should. As Brazil has learned the hard way in confronting the car wash scandal, for the best government, transparency **must** be made pervasive at all levels of government.

The Brazil Arbitration Act was designed to instill and protect this virtue, providing at Article 2 specifically that "arbitration that involves public administration . . . will be subject to the principle of publicity". Well done, you Brazil government lawyers!

If true wisdom, conventional or otherwise, leads you to choose arbitration as your dispute resolution alternative, your work in securing its advantages begins with the drafting of the arbitration clause covering an entire contractual relationship, or drafting the clause in creating the basis for *ad hoc* arbitration after a dispute has arisen. Your draftsmanship is of the greatest importance, because what is most distinctive about arbitration as a modality of dispute resolution, is party autonomy. That is, in contrast to judicial litigation, the parties choosing arbitration can control the entire process, depending upon how the agreement to arbitrate is drafted. The parties determine by consent; jurisdiction, procedure, and the substantive law that

governs both the arbitration process and the determination of the merits of the dispute. The parties can designate the applicable law, both substantive and procedural. They can choose the law to govern the arbitration process, and are free to choose the same or different substantive and procedural principles for determining the merits of the dispute.

So there are many choices to be made in your drafting. Should the arbitration be left *ad hoc*, to be agreed, if at all, once a dispute arises, or agreed as part of the greater deal? Should arbitration be designated to occur under the aegis of an arbitral institution and/or its rules? That is, to what extent do you want utilize a potentially expensive existing arbitral institution and its rules, or maintain more robust and complete control over the procedural and substantive issues – though going it alone *ad hoc* may require reinventing the wheel, and may heighten the risk of leaving out something important? What should be the scope of the arbitration as to jurisdiction including substantive issues? What should be the remedial authority of the arbitrator, the applicable procedural and substantive law for the arbitration?

What law should govern the merits of the dispute, how different than the law designated to govern the procedural and substantive standards for conduct of the arbitration itself? Should a time frame and/or time limits be specified? Should the parties empower the arbitrator to interpret or clarify its award, for example as was done in an international arbitration I will shortly discuss, the arbitration between Israel and Egypt concerning a dispute over the Taba territory in the Sinai? Should the arbitrator be authorized to resolve future related disputes, as was done for the Rainbow Warrior controversy between New Zealand and France?

In my practice as an arbitrator, and in studying the cases, I have always found it remarkable how commonly lawyers fail to address such basic questions that should best be resolved when adopting arbitration and drafting the arbitration clause. This reflects a general lack of awareness of the significance of the content of the arbitration clause; until it is too late.

Consider one example of this sort of lawyer negligence, where the lawyers left out just about everything, but were nevertheless compelled to arbitrate. This was a significant governmental arbitration that took place in San Francisco in the early 1980's concerning the very substantial matter of debt obligations of the then newly in power Sandanista government of Nicaragua. That government sought to compel arbitration of its expropriation of a fruit company, one of the US enterprises that had previously dominated the Nicaraguan economy. Meeting in San Francisco, the lawyers on both sides of the dispute thought they had achieved a settlement. But the deal was never finalized, and contracts never executed. However, the lawyers had vaguely agreed to arbitrate disputes. The agreement to arbitrate was wholly deficient, with virtually nothing specified. The lawyers couldn't even remember the name of

the London arbitration agency some of them thought they might use, so they didn't designate an arbitral forum. Nevertheless, the US Ninth Circuit Court of Appeals sitting in San Francisco determined that arbitration was required, on the basis of the strong US federal policy in favor of arbitration, and the related so-called 'severability doctrine". That doctrine provides that though a contract may be held to be invalid or never even consummated, if arbitration was agreed, arbitration will be treated as severable and enforceable. You need to be aware that same doctrine is now also the law of Brazil under Article 8 of the Brazil Arbitration Act. Particularly as a government lawyer, where the statement of jurisdiction or choice of arbitral forum or applicable law may be critical, you therefore surely need to concentrate on such important considerations in drafting your arbitration clause.

The example I've just recounted is what commonly occurs. When lawyers are negotiating an agreement, they focus on making the deal, not the dispute resolution that might be engaged if the deal falls apart. Normally, so long as they are not thinking about arbitration, there really isn't all that much to think about, since the existing litigation system is a given. As trained lawyers, you assume the details of the dispute resolution process of court litigation. So for the lawyers intent on the deal, not much may be thought or said about dispute resolution, unless someone puts arbitration on the table. And even with that, arbitration is often treated as a minor matter, an option, often at best, an afterthought – especially where it has been late in arriving in the array of dispute resolution experience, as in Brazil.

But arbitration is profoundly of significance in opening the design of the dispute resolution process to the parties creating their own legal system – the foundational principle of arbitration being 'party autonomy'. If the lawyer doesn't do the preparatory work required to secure his client's interests in designing the arbitration, the lawyer will have missed the boat that's already sailed. If the boat later sinks with your client's cargo, the lawyer is poorly positioned to deny responsibility. The truth of the matter is that when things go wrong, the arbitration agreement, however ill-formed, may likely become the most important clause in the contract. So it is imperative that you do the necessary preparation, when you are thinking of engaging arbitration; that you give full consideration to drafting the arbitral regime by way of the arbitration clause, in all its critical aspects.

## III. Waiver of Governmental Prerogative.

The drafting of the arbitration clause is important for any contract, whether or not government is involved. But what are the critical aspects for a government lawyer considering arbitration?

First be aware, that by engaging arbitration you may be waiving powers, defenses or rights that are unique to government. This is especially so as to otherwise viable claims of sovereign immunity. Brazil, along with all countries fully engaged in the global economy, has adopted the restrictive theory of sovereign immunity, meaning that immunity can be claimed when the nature of governmental action involved in your matter can be characterized as 'public', from Roman law, *ius imperium,* but not for governmental activity characterized as 'commercial' or 'private'. (from the law of Rome, *ius gestionis*) This principle is now in article 37 of the Brazil Arbitration Act. Brazil law has also adopted the related 'principle of legality' whereby arbitrability is limited to 'relevant assets', that is, economic, and 'disposable rights' (rights of a commercial, economic or financial nature) as distinguished, for example, from matters such as family law or labor rights. Also reflecting the protection of public rights and assets is that their disposition, under the law of Brazil, is said to require special legal authorization.

But for matters of any complexity involving public and private interests, whether the dispute is deemed 'public or private', often depends on simply how a judge or arbitrator characterizes the facts. This is well illustrated by a case that went before the United States Supreme Court. The plaintiff was a US citizen who was hired by Saudi Arabia in the US to monitor safety at a Saudi hospital. While working in Saudi Arabia he was thrown into a Saudi prison and physically abused when he actually did the job he was supposed to do, and flagged safety violations that embarrassed one or more of the ruling Saudi princes. The Supreme Court of the United States concluded Saudi Arabia was immune from suit, because what was involved was Saudi police action being characterized as public activity. This was despite the fact that the plaintiff's hiring was a commercial contract, i.e., clearly "commercial activity", and that the contract was negotiated and signed in the United States.

As this case well illustrates, the immunity determination is highly manipulable. It turns on which facts the Court chooses to make the basis for its public or private determination. The choice, as this case also demonstrates, is often made for political reasons. It was no accident that the claim of Saudi immunity was upheld, within the same time frame that the Saudis allowed US forces to be located on Saudi soil for the first Gulf war.

However, and nevertheless, it is essential for government lawyers to understand, that the contractual adoption of an arbitration clause, entirely pre-empts the issue of immunity. In US domestic law, and in general in international arbitrations, an agreement to arbitrate is

read broadly by courts as a waiver of any possible claim of immunity. The pendulum has swung so far in this direction, that in 1988 the United States Congress passed a statute that specifically provides that if a government or government agency has agreed to arbitration – the agreement to arbitrate completely eliminates sovereign immunity from the dispute, whether as a defense or otherwise.

So the instruction for a lawyer representing a government or government agency is; never agree to arbitration without fully assessing your potential claims for immunity, or other special rights of a governmental entity that may be thereby waived.

## IV. Political Deflection.

Related to sovereign immunity is the consideration that, usually, the more significant the government interest involved in a dispute, the less government should take the risk of casting its fate to a third party neutral by agreeing to arbitration. Thus Colombia and Venezuela were willing to arbitrate a territorial dispute, but not maritime boundaries in the Gulf of Venezuela after discovery of oil reserves there in the 1960's. One technique, however, to still enjoy the benefits of arbitration in matters of such significance, if it can be accomplished, is to break up the dispute into its components, resolving the lesser for arbitration and the greater for negotiation.

But the smartest strategy, in the right case of high profile governmental interest, may be quite the contrary – to adopt arbitration for resolution of the entire dispute. This is a strategy I call 'political deflection'. The right dispute for this strategy, is when the dispute, as an American colloquialism expresses it, is "too hot for diplomacy to handle".

Consider two examples from international arbitration – the arbitration between Israel and Egypt concerning jurisdiction over the Taba area on the coast of the Sinai Peninsula, and the 'Georges Bank' dispute over fishing rights on the adjoining coasts of Canada and the United States. Both were situations where the dispute was so hotly loaded with the economic and political interests of domestic constituencies, that diplomacy was not likely to succeed. For the case of Taba, the symbolic significance of any conflict of jurisdiction between Israel and Egypt was too great for diplomatic resolution, given the history of conflict. For the Georges Bank Arbitration, which concerned, on the one side the interests of Canadian fishermen, and the other the interests of United States fishermen, a concession by either side would have been viewed as a betrayal of its fishermen. In both Taba and the Georges Bank any diplomatic

compromise would have inevitably left the domestic constituencies blaming their government for failure to adequately vindicate their rights. But by moving the matter to the neutral third party process that arbitration affords, however, the governments of Israel, Egypt, Canada and the United States, in response to any result less than 100%, could all proclaim to their domestic constituents, “we did the best we could. It was that incompetent arbitrator who failed to fully vindicate your rights”.

It is thus that arbitration can be utilized as an escape from political accountability. And why not? Our subject today is successful dispute resolution. If such political deflection is what it takes, so be it.

## V. Party Autonomy and Public Policy.

Beyond these matters of strategy in selecting arbitration from among dispute resolution alternatives, a government lawyer should be aware of the serious consequence of party autonomy in affecting the mindset of an arbitrator. Arbitration is likely to be much less sensitive to the concerns of government than litigation before a judge. This is because the social legitimacy of arbitration is based exclusively on the parties consent, not national sovereignty. For an arbitrator, the standard of the decision is the contract. Judicial litigation,

to the contrary, while considering the contract, makes preeminent the interests of the state.

The arbitrator’s preoccupation is what did the parties intend their contract to mean. A judge on the other hand, is not just interpreting the contract, but is doing so guided by concerns of public policy reflected in statutory or regulatory law, or the relatively amorphous concepts of public policy and good morals. A judge, as a government official, has the responsibility to secure the mandates of the law and the integrity of the official legal system. Yes, the judge looks to the intent of the parties, but gives priority to the mandates of the law with awareness that whatever he or she decides, will be a matter of precedent for the future of society and for similar disputes to come. The judge is also aware that any decision he or she renders is subject to reversal if found at odds with the letter or policies of the law. In judicial litigation, the judge writes for other judges, developing the law. The judge is concerned with the institutional duty to the legal system, and perhaps above all, the very personal and

professional concern not to be reversed. In that regard, judicial litigation has a more conservative inclination in its results. The formality and procedural requirements of judicial litigation in comparison to arbitration also make it more likely that the litigation judge will be restrained by established norms than will the arbitrator.

The arbitrator by contrast to the litigation judge proceeds unencumbered by precedent, not concerned about making it or following it, nor by acting contrary to established standards. The arbitrator is accordingly freer to take on a legislative role and shape the dispute to the interests of the parties at hand. This is especially because the arbitrator can do so without fear of review, given the relatively very narrow and limited grounds for reversal of an arbitral award.

The Brazil Arbitration Act as amended recognizes this potential deficiency in public policy sensibility of the arbitrator compared to the litigation judge. Article 2 of the Brazil Arbitration Act provides that the rules chosen by the parties to govern their arbitration must not violate "good morals and public Policy". Article 39 additionally provides that a foreign arbitral award cannot be recognized or enforced if "the decision violates national public policy". In making such provision Brazilian law is consistent with the public policy limitation on enforcement as stated in the NY Convention, and is similarly consistent with the public policy defense as stated and administered in virtually all arbitration regimes.

However, the actual record of arbitrations, both national and international, belies the effectiveness of any such attempt to establish a public policy limitation. Public policy is rarely invoked with success to prevent the rendering or enforcement of an arbitral award.

This has been dramatically demonstrated in US law with respect to our antitrust laws. These are the laws that the US Supreme Court has referred to as our "Charter of liberty"; of importance just below the US Constitution. Most commentators therefore thought implementation of the antitrust laws to be off-limits for domestic arbitration, and especially for international arbitration, which could remove public policy control completely from the United States. Then, after international arbitration was deemed to be legitimately advantageous in a broad range of US federal statutory areas, including the securities laws and labor laws, came the big test everyone was waiting for  anti-trust, where US policy was uniquely firm and extreme compared with most other nations.

The case that tested the impact of arbitration on antitrust had been filed against the Japanese Mitsubishi car company, under contract with a US distributor provided for arbitration in Japan, and violation of US antitrust law was a central claim in the dispute. The United States

Supreme Court, nevertheless, declared the provision for foreign arbitration valid and enforceable, much to the surprise of the international arbitration community.

The consequence, therefore, of the party autonomy principle of arbitration under US law, is that even the most significant public policy, even if embodied in the most important statutory law, can be made subject to arbitration. Today, not only Mitsubishi, but other cases both in the US and elsewhere, instruct that public policy as a limitation on arbitration, is not much of a limitation at all.

One reason for this is simply that burdened courts get to love arbitration. My own experience is that any time a lawyer challenges the scope of my jurisdiction as arbitrator, I respond, "So take it to court. Maybe we'll save time that way, as you suggest, though I think not. We will reconvene once the court rules on whether I have jurisdiction". The result, invariably, as I expect, is that the judge prefers that the arbitrator do the work. The court reads my jurisdiction as broadly as possible, and we reconvene with full jurisdiction of the arbitrator judicially confirmed.

Another reason the courts are inclined to read the jurisdiction of the arbitrator as broadly as possible is -- as previously noted when I spoke of the greater admission of evidence in arbitration - that there is no deduction from the judge's salary for the lesser work resulting for the judge deferring to arbitration. The judge is paid by the state at a fixed salary, no matter the lesser or greater his or her caseload. But the arbitrator bills by the hour, or by the day. So judge and arbitrator alike are content with the broadest reading of arbitrator jurisdiction, notwithstanding the enhanced risk that public policy will be ignored in arbitration. For public administration arbitration, therefore, often the only safety, the only control, is that responsible government attorneys, such as yourselves, will protect the public interest and public trust, by declining to agree to arbitration where the public interests or other third party interests are substantially at risk.

The ostensible control of 'public policy' is even less consequential at the enforcement stage of arbitration than when asserted as basis for 'non-arbitrability'. Though the Brazil Arbitration Act, the New York Convention and most other arbitration formulations provide for public policy or 'good morals' as basis for non-enforcement or annulment of an arbitral award, these doctrines are rarely employed, and rarely successful. In the Mitsubishi case the US Supreme Court said the public policy mandate of the anti-trust laws could be guaranteed because at the time the prevailing party would seek enforcement of the award, the reviewing

court could check whether the US antitrust laws had been taken into account by the arbitrator, and if not, deny enforcement. But given that an arbitral award is most often in the form of an amount of currency to be paid, or a denial of any compensation, this claim of control is pure fiction. How would a reviewing court determine whether a number or zero, the typical antitrust result, represents the arbitration having taken into account the antitrust laws? And of course, the arbitrators, who now know that the US Supreme Court's Mitsubishi decision could be a basis of reversal of his or her award if the anti-trust laws are ignored, need simply state in its award that the arbitration did take into account the antitrust laws to protect their award.

Furthermore, though in the past many US courts were inclined to reverse when there was so-called 'manifest disregard of the law', "manifest disregard of the law" is no longer generally recognized as a valid objection to recognition and enforcement of an arbitral award. This is another consequence of favoring arbitration for its value in achieving expeditious finality.

So there are a number of reasons why judges are inclined to leave it all to arbitration, despite what may be their better instincts for protecting the public interest. Indeed, the grounds for review and reversal of an arbitral award are so limited, and the inclination of judiciaries to avoid any review of the merits so strong, that the ultimate result of party autonomy and independence of the arbitrator, is that the arbitrator, as an Administrator of the AAA in San Francisco has expressed it, is a "500 pound gorilla". Arbitration is a 500 pound gorilla because the arbitrator need not worry about reversal on the basis of public policy, so as long as there is no demonstrable bias, offense to due process, or lack of jurisdiction – all rarely successful grounds for reversal.

And therefore the instruction for your representation of government is that by choosing arbitration over judicial litigation, you run a significant risk that public policy or good morals will fall outside the purview of the arbitrator, who is focused primarily, and most often exclusively, on what the parties intended by their contract.

Be cautious, then, about adopting arbitration. Here is your typical arbitrator -- -that 500 pound gorilla. (first gorilla picture, titled 'Arbitrator'). Don't be misled by the suit he's wearing. Here is the real guy, complete in his naked truth and glory. (second gorilla picture, titled 'Arbitrator Revealed'). I hope you see you need to be very careful before you invite this guy to mess with your practice of the law and your protection of the public trust. If the dispute importantly concerns public policy of the state, rather than simply contractual rights – beware of the arbitrator.

The Brazil Arbitration Act recognizes and does attempt to avoid the risk to public policy that arbitration presents. For arbitration involving public administration, the Brazil Arbitration Act specifically prohibits arbitration from ignoring the mandate of the law. It provides at Article 2, paragraph 3, that "arbitration that involves public administration will always be at law", thereby rejecting equitable discretion, known to dispute resolution in reference to its Roman origin, as *ex aequo et bono,* roughly translated, as acting according to the fair and the good, first developed in Roman law for guidance of the Roman magistrates. The Brazil Arbitration Act rejects any such subjective power for the arbitrator. It provides at Article 26 that the arbitral award must contain "the grounds of the decision with due analysis of factual and legal issues". Presumably this requirement, for a so-called 'reasoned award', is also there to assure strict adherence to the law, and any public policy mandate of the law.

For arbitration involving government, the Brazil Arbitration law thereby purports to preclude any exercise of equitable discretion by the arbitrator, despite the fact that equitable discretion of the arbitrator to act *ex aequo et bono* is recognized as legitimate in most arbitral systems, not only in the private sector, but also in international arbitration that includes governments and their agencies. Particularly in international arbitrations involving governments, *ex aequo et bono* thrives, valued as assuring the flexibility of decision to frame a result as 'fair' for both parties, instead of being compelled to designate winner and loser, as the litigation judge most often must do. Such discretion of the arbitrator is also valued as providing the flexibility to adjust to changed circumstance, and make provision to avoid future conflict.

But does the Brazil Arbitration Act truly eliminate the potential for the 500 pound gorilla to ignore the public policy mandate of the law, in favor of his or her notion of what is fair? It does not, simply because there is no review on the merits of an arbitral award. A prohibition of *ex aequo et bono* can be ignored by the arbitrator without penalty, because there is no review on the merits. The arbitration may well state reasons for its award, as required under Article 26 of the Brazil Arbitration Act, but there is no way to prevent the arbitration from actually employing equitable discretion in making its award. Arbitrators, universally, render their awards with full awareness their awards cannot be reviewed and reversed on the merits. It is the very nature of arbitration to provide this assurance. The assurance of no review on the merits is what distinguishes arbitration as providing greater and more expeditious finality than judicial litigation, or negotiation, or mediation.

There is ultimately, therefore, a contradiction and tension under the law of Brazil between the prohibition on the exercise of equitable discretion for public administration, and

the limits of review. The Brazil Arbitration Act attempts to accomplish the impossible – requiring decision exclusively at law, while still providing what arbitration most importantly provides – a guarantee of expeditious finality.

The instruction for you as a government lawyer is therefore – don't be misled by the Brazil Arbitration Act's prohibition of equitable discretion. *Ex aequo et bono* is still there, alive and well, but as an even more threatening discretion of the decision-maker than in litigation. The arbitrator's subjective sense of equity can affect the admission of evidence, the cross-examination of witnesses, examination of documents, and most importantly, the result. In arbitration, *Ex aequo et bono* is not in the controlled hands of a judge subject to judicial review, but in the uncontrollable hands of this guy, the 500 pound gorilla.

## VI. Neutrality.

But even recognizing the arbitrator's power includes uncontrolled discretion even where prohibited, does arbitration after all assure neutrality? So what if the arbitrator assumes the power to do equity, isn't 'fairness' the worthy objective no matter however great the arbitrator's discretion in rendering judgment.

First to be recognized is that party autonomy means that if there is inordinate leverage between the parties that results in the choice of arbitration, it can naturally lead to unfairness as to any procedural or substantive aspect of arbitration. For example, the health care contracts of the Kaiser System in California used to provide that only Kaiser doctors could act as arbitrators. Besides the obvious problem of inherent bias, it resulted that delays in the system engineered by the doctors in their self-defense, allowed an inordinate number of patients to die before there could be arbitration of their claims. Similarly, US investment houses provide that arbitrators in securities cases were required to be members of the National Association of Securities Dealers. To the same unfair effect, consumer contracts leveraged by large consumer product producers include arbitration clauses with waivers of class actions and punitive damages, making economically unsupportable the pursuance of consumer claims. To the same effect, certain industries, applying their leverage against employees and labor unions, insert clauses to limiting labor complaints to arbitration, thereby constricting labor rights.

Here Brazil's law is marked by the failure to counter such inherent bias. In 2015 the President of Brazil vetoed the bill that would have avoided similar invitations to unfairness. The vetoed provisions would have required a worker or a consumer to confirm the choice of

arbitration by personal authorization post-cotract, before being bound by any contractual consent to arbitration.

An even more insidious unfairness can result from the economic interest of the arbitrator harnessed by a party who present the implied promise of repeat business as the reward for a favorable result. The implicit economics of a dispute involving the arbitrator with a once-only party on the one side, and the potential repeat customer on the other, may well bias the result. This typically means favoring the large over the small, the company over the consumer or employee, and even the state over its citizens. I personally had an interesting experience in this regard, when I ruled against a California state agency, and that agency then pulled all its disputes business away from the American Arbitration Association because I did not comply with the entitlement the state agency thought should result from their repeat business.

## VII. Interagency Arbitration – The Model of the NAFTA Side Agreements on Environment and Labor.

Finally, I want to suggest a special formulation of arbitration that you may find of value for future planning for governmental interagency arbitration. Governmental interagency arbitration deserves special consideration because it is comprised of governmental interests and public policy concerns on both sides of the dispute, and ongoing intergovernmental relationships. My suggestion, that takes this important aspect into account, is to consider the model that was developed to secure the NAFTA Treaty approval, despite resistance from labor and environmental constituencies. That model is the NAFTA Side Agreements on Labor and the Environment.

I've authored an article providing a detailed analysis of this unique model if you would be interested in any further elaboration than the time for my talk here allows. That study was published in the American Journal of International Law. Anderson has informed me his office can it make available to you, upon request, by electronic copy.

But the essentials can be stated briefly. The scheme is to begin dispute resolution with negotiations at the highest governmental level available, then to proceed to arbitration if those negotiations do not resolve the dispute, but to have the arbitrators provide not an award, but their proposal for a mutually satisfactory action plan. If the complained against party rejects that plan, that party then has the burden of proposing its own solution, which the arbitrators can accept or reject. If the arbitrators reject it, the failure of the complained against party to comply

with the arbitrator mandated plan, through the end of the process, can result in sanction, first by fine, and if that doesn't secure the arbitrator plan, ultimately a loss of trade benefits. This design incorporates a number of opportunities to negotiate along the course of this process, which is supposed to take a maximum total of 1225 days.

The uniqueness and advantage of this model is to achieve a fusion of political and legal process. It maximizes the expression and accommodation of the political interests of the parties, while providing continuing opportunity for consensual resolution. Arbitration is employed more to drive the process of resolution than to provide an award, more to educate the parties concerning constructive resolution and enforce that outcome if necessary. The objective is to avoid the need to reach the ultimate sanction of loss of trade benefits, a result that would be counterproductive to the very purpose of NAFTA. It is a design that acknowledges the political reality that it is the governmental parties who best understand the respective interests they represent, but engages arbitration to compel the parties to find a practical solution. It is a design that maximizes the capacity of arbitration, in contrast to litigation, to achieve a solution instead of a winner. Presumably that would be the most desirable end-game for interagency arbitrationin Brazil as well, which is why I am proposing it for your consideration

**VIII. Cultural Awareness.**

**IX.**

My final point about what's special about arbitration involving government, but by no means least significant, is the importance of cultural sensitivity. Cultural sensitivity is more important for government attorneys considering the choice of arbitration, than for private sector attorneys, because of the different interests they represent. In commercial arbitration, the parties, their attorneys and the arbitrator, generally represent a homogeneous cut of the national population, whether measured in terms of education, professionalism, or social class. In other words, commercial arbitration, being commercial, is mainly about wealth - - - those who enjoy the advantages of wealth, and those who have enough wealth to afford to be fighting about it through legal process and lawyers. However, in arbitration involving government, the government lawyer represents the diverse interests of society at large. The client base, for a government attorney, in the ultimate respect of citizenship, includes not only the wealthy and educated, but also the poor and middle class populations, many without the advantage of being able to employ lawyers to handle their disputes, most isolated and alienated from the legal system.

These people are isolated and may be alienated, except as represented by you, the government lawyer, in defending and enforcing the public trust. Your challenge as a lawyer requires working on behalf of a much more diverse population of interests than the private commercial attorney. And the greatest challenge, is representing those members of society who are more outside the legal system than within it, except when they get in trouble. The need for legal representation of the thus disenfranchised and disabled presents as great a challenge in Brazil and the United States, as it does in the rest of the world, given the well documented increasing disparity of opportunity everywhere on our planet, between those who have and those who have not. The consequence is a greater responsibility for the government lawyer in arbitration, and that respondiblity includes special sensitivity to the variety of cultures and constituencies you represent.

I learned about the importance of cultural sensitivity most pointedly in Rio some years ago. Please indulge me a story about cultural difference, which may seem trivial, but I think makes the point. Anyway, *I* learned from it, and hope you find it instructive. Ironically, at the time of the event that taught the lesson, I was in Rio as the professor placing my students in law firms, with the assistance of the then private lawyer, Anderson Schreiber. However, it was Anderson, the then private lawyer, well before his distinguished academic and public service, who taught me the relevant lesson.

There we were in the middle of downtown Rio, in Anderson's car, waiting at a stoplight at a major intersection, when a Rio public bus swung around the corner and smashed into us, tearing the door off Anderson's car. (Here's a picture of the common fate of cars encountering Rio buses, although thankfully, the bus didn't eat nearly as much of Anderson's car as it did the car in this picture.)

Immediately, there was considerable commotion, and soon the police arrived. The police proceeded to have all the passengers descend from the bus, and then to interview each passenger, about 30 of them, taking a long statement from each, one by one. After about an hour of this, I grew impatient, as any North American would be likely to do, and I asked Anderson, "why isn't it like the US, where for a vehicle collision, the policeman simply produces his report based on what he observed and the interview of, at most, in a situation like this, a couple witnesses?" Anderson replied it was necessary for each Carrioca to have his or her say about the collision. After another hour and a half of the interviews, I reached the end of my patience. Distraught at what seemed a crazy delay, I asked Anderson, "shouldn't this be simple? We were sitting here at the light. The bus slammed into us. What is the issue? The bus is clearly responsible. What in the world do they all keep talking about? What could they

possibly be talking about for so long?" Anderson paused, and with a solemn expression, and a one word answer worthy of Confucious, or The Buddha, he replied, "Nothing"

Gustavo Tepedino once gave me a key to appreciating the joyful Carrioca culture of Rio, telling me, "here, a straight line is not always the shortest distance between two points, but we get from here to there". Viva the cultural differences that make it all so interesting! Nevertheless, I hope I've presented you something more than nothing, and I thank you for your patience in listening to my talk, though it didn't go in a straight line. But being back in Rio with old friends and great memories restored, I have taken the liberty of considering myself an honorable Carrioca.