The evolution of the interpretation of the Competence-Competence principle in the Brazilian Legal Order: legal certainty provided for foreign investors

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Abstract: This article seeks to contribute to the understanding of the application of the Competence-Competence Principle to contracts that provide for arbitration clauses by different jurisdictions and Brazilian Courts. This study was mainly motivated because of the recognition by the Brazilian Superior Court of Justice of the applicability of the Competence-Competence principle to concession contracts, despite the existence of a public interest in the case. The decision provides legal certainty and better environment for foreign investors doing business in Brazil, especially in the energy sector.

Keywords: Competence-Competence Principle. Arbitration. Concession Contracts. Public Interest. Brazil.

Introduction

This study analyzes how the Competence-Competence principle, which is one of the most important principles in the arbitration outlook, has been applied by different jurisdictions worldwide. This article focuses on the roles conferred on courts and arbitration tribunals for resolving disputes over arbitral jurisdiction, shedding light on the Brazil legal framework and on its highest court interpretation as regard the applicability of this principle.

This article was motivated primarily by a recent decision rendered by the Brazilian Superior Court of Justice ("STJ") in a great dispute between the Brazilian semi-public multinational oil and gas company, Petróleo Brasileiro S.A. – Petrobras

("Petrobras"), and the Brazilian National Agency of Petroleum, Natural Gas and Biofuels – ANP ("ANP"), by which STJ recognized the applicability of the Competence-Competence principle over concession contracts, despite the existence of a public interest in the case.

The importance of this decision is not limited to the Brazilian legal order, as it confers on the international investors' legal certainty over the arbitration agreement applicability, and thus provides proper conditions for foreign investments not only in the oil and gas sector, but also in all sectors where the public interest is present.

1 Competence-Competence principle in the International Arbitration

1.1 The Competence-Competence principle doctrine

One of the most relevant questions related to arbitration is who is entitled to decide on the existence and the validity of the arbitration agreement, whether the arbitration tribunal or the local courts where the dispute has arisen. This issue is crucial for the efficiency and attractiveness of arbitration as a dispute resolution process.

The Competence-Competence principle[1] plays an important role in determining who may decide the issues and which standard is applicable. This principle is one of the founding principles of international arbitration law,[2] and confers on the arbitration tribunal jurisdiction to rule on its own jurisdiction when the validity or scope of the agreement to arbitrate is challenged. Hence, as a consequence, the parties are not required to ask a court to resolve jurisdiction questions.

This principle was incorporated in International Arbitration by the New York Convention of 1958,[3] which sets the main rules for the principle,[4] and imposes on contracting states, including Brazil, the obligation to enforce arbitration agreements.

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1 The English term "competence-competence" is derived from the German term "Kompetenz-Kompetenz", known in French jurisprudence as "compétence de la compétence". In each case, the term refers to the tribunal's jurisdiction to decide its jurisdiction. (Park, W.W. (2008). Arbitral Jurisdiction in The United States: Who Decides What? *International Arbitration Law Review, 1*, 37).

2 Regarding this questions, see Gaillard, E. & Banifatemi, Y. (2008). Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. *In Enforcement of Arbitration Agreements and International Arbitral Awards – The New York Convention Practice*, ed. E. Gaillard & D. Di Pietro (p. 258). London, UK: Cameron May.

3 Convention on the Recognition and Enforcement of Foreign Arbitral Awards, entered into force on June 7, 1959, hereinafter the "New York Convention." At the time of the elaboration of this article, 157 States were parties of the New York Convention. Retrieved December 1, 2017, from http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html.

4 The New York Convention of 1958 was developed based on the work established by the Geneva Protocol of 1923 on Arbitration Clauses, the Geneva Convention of 1927 on the Execution of Foreign Arbitral Awards, and by the request in 1953 by the International Chamber of Commerce to the United Nations Economic and Social Council to convene on the subject of enforcement of international arbitration judgments. The New York

The Competence-Competence principle is expressed in Article II:3 of the 1958 New York Convention, which provides:

> The court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed.

However, national courts may not refer parties to arbitration where "[a court] *finds that the said agreement is null and void, inoperative or not capable of being performed*." This provision – provided for in Article II:3 of the New York Convention – therefore implies that the arbitration agreement could be subject to interlocutory court review before, or simultaneously with, the arbitral proceedings.

Following this reasoning, the New York Convention does not allocate jurisdictional competence as to an arbitration agreement as between the arbitral tribunal and the relevant national courts. In consequence, as each legal system implemented the principle of Competence-Competence according to their own national laws, two questions turn out critical, according to HOWARD HOLTZMANN and JOSEPH NEUHAUS: i) when can a court review be applied? – and, ii) what is the extent of such a review?[5]

This principle is widely codified into national arbitration laws and institutional rules, and sometimes it is supported by the separability principle (or severability), which cannot be jumbled with the former, confers on an arbitration clause a distinct treatment from the contract, allowing the clause, and therefore jurisdiction, to survive invalidity or termination of the contract. That is to say that, even if the arbitrator concludes that the contract is invalid, it is not considered without competence to decide on the matter, in light of PETER SANDERS statement.[6] The justification for this reasoning lies in the contradiction that would consist in allowing the interference of the local courts on issues arising from contracts where the parties had previously agreed to submit them to an arbitration tribunal.[7]

Convention was also drafted as a response to the great demand for commercial arbitration by international businesses willing to obtain the advantages of arbitration. (Cole, R. A. (1986). The Public Policy Exception to the New York Convention on the Recognition and Enforcement of Arbitral Awards. *Journal on Dispute Resolution*. (V. 1:2), p. 368).

5 Holtzmann, H. M., & Neuhaus, J. E. (1995). A Guide to the UNCITRAL Model Law on International Commercial Arbitration. Legislative History and Commentary (p. 303). Kluwer Law International.

6 Peter Sanders states that the separability principle refers to the arbitrator as competent to decide on whether the contract is null or void, notwithstanding the contract is null since its outset. (Sanders, P. (1999). Quo Vadis Arbitration? Sixty Years of Arbitration Practice. A Comparative Study (p. 33). Kluwer Law International).

7 Diamvutu, L. (2009). *The Competence-Competence principle in Voluntary Arbitration* (pp. 2-3). Retrieved from http://www.fd.ulisboa.pt/wp-content/uploads/2014/12/diamvutu-lino-o-principio-da-competencia-competencia-na-arbitragem-voluntaria.pdf.

It is relevant to point out that the wide acceptance of the 1958 New York Convention, which has benefited the recognition of the international arbitration worldwide, has extended its protection to parties' agreement to settle their disputes before an international arbitration.

Regarding this understanding, EMMANUEL GAILLARD and YAS BANIFATEMI address that "*the basic requirement that the parties to an arbitration agreement honor their undertaking to submit to arbitration any disputes covered by their agreement entails the consequence that the courts of a given country are prohibited from hearing such disputes*".[8] Therefore, if a court encounters a matter subjected to arbitration, even if the submission to arbitration is being contested by an involved party, it must refer the parties to an arbitration tribunal.

The Competence-Competence principle, in sum, empowers arbitrators to decide, prior to the courts (known as the negative effect of the principle of Competence-Competence), on both their own jurisdiction and the validity and scope of the arbitration agreement, as demonstrated below, to the development of the arbitration process, and thus to strengthen the legal certainty, with important consequences to the attraction of foreign investments.

2 Who decides first the competence?

2.1 The positive and negative effects of the Competence-Competence principle

The Competence-Competence principle has a dual function, referred to as positive and negative effects, which drives the arbitration process.

The positive effect of the Competence-Competence principle relates to rules conferring to an arbitral tribunal jurisdiction to decide on the validity and scope of an arbitration agreement.[9] In both national and international arbitration law it has empowered an arbitral tribunal to rule on its own jurisdiction, despite the fact that it is not a permanent body as the national courts are.[10] As stated by Emmanuel Gaillard and Yas Banifatemi,[11] challenging the existence or validity of the arbitration agreement will not halt an arbitration. Nonetheless, any court aims to decide on the merits of the dispute in question, once the arbitrator has retained

[8] See Gaillard, E. & Banifatemi, Y. Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. at 257.

[9] Ranzolin, R. (2002). *Controle Judicial da Arbitragem* (p. 140). Rio de Janeiro, Brazil: GZ Editora.

[10] See Gaillard, E. & Banifatemi, Y. Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. at 259.

[11] *Id.*

its own jurisdiction, it will proceed with the arbitration rendering a decision on the merits of the dispute.

The positive effect is accepted by the international law and by all countries which recognize arbitration as a legal method of dispute resolution, without any controversy due to its respect.

Unlike the positive effect, the negative effect is more controversial. As stated by EMMANUEL GAILLARD and YAS BANIFATEMI, the rule of priority in favor of the arbitrators takes the Competence-Competence principle a step further than its positive effect by providing to the arbitral tribunal priority in the analysis of its own jurisdiction. It confers a negative or restraining effect on the domestic court, which must refrain from rendering a decision regarding the questions related to the existence or validity of the arbitration agreement prior to arbitrators. The role of the court is hence, deferred to subsequent review of the arbitral tribunal's decision.[12]

The reasoning of a subsequent review of the arbitration's decision by the court is justified as a measure to prevent obstructing and delaying the progress of the proceedings by the parties, which, for tactical reasons, may aim to raise issues regarding the existence and validity of an arbitration clause, despite their previous acceptance of its insertion in the contract. For instance, despite its prior acceptance of the arbitration clause, a party, usually in the position of respondent, may prefer to have the case judged by the court rather than by the arbitral tribunal, because in many jurisdictions the latter proceedings are quicker than the former. This is just one example of an attempt by a party to challenge an arbitration agreement.

Consequently, if it was conferred to a party the possibility to challenge the validity of an arbitration clause before the court, the arbitration proceedings could be delayed for months or even longer. Moreover, the costs and potential losses of the rights borne by a party would be better preserved if not admitted the coexistence of parallel and duplicative proceedings on the question related to the existence and validity of the arbitration agreement.

The rule of priority in favor of the arbitral tribunal has been increasingly recognized in practice, in accordance with the nature and autonomy of international law, and the New York Convention philosophy of recognition of the arbitration agreement and, also of validity and enforcement of its final award. In fact, the more international arbitration is viewed, the less interventionist in its proceedings the court will be, by applying the negative effect more firmly.[13]

[12] See generally Gaillard, E. & Savage, J. (1999). Fouchard, Gaillard, Goldman on International Commercial Arbitration (p. 401). Kluwer Law International.

[13] See Gaillard, E. & Banifatemi, Y. Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. at 269.

2.2 Is the arbitrator's decision ever subjected to judicial review?

As stated by Emmanuel Gaillard and Yas Banifatemi, recognizing the arbitrator's priority in the determination of their own jurisdiction does not mean that the domestic courts waive their power to review the existence and validity of an arbitration agreement.[14]

The priority conferred to arbitrators' – consistent with Article II:3 of the New York Convention – means that, when "*making a prima facie determination that exists in an arbitration agreement and that it is valid*",[15] the domestic courts leave the arbitrators to rule the question, but they recover their power of full scrutiny after the award is rendered by the arbitral tribunal.

As a consequence of the negative effect, the arbitrators have the *priority* to decide on their own jurisdiction. That is to say that their competence to decide whether it has jurisdiction over a case brought before the arbitration court *precedes* (as opposed to the *sole*) the state's jurisdiction.

Thus, due to the consequence of the negative effect, the courts having jurisdiction to review arbitral awards in the limited exceptions permitted by the New York Convention, provided for in Article V, have jurisdiction to review the existence and validity of an arbitration agreement.

2.3 The recognition of the rule of priority by local courts

The rule of priority in favor of the arbitrators has been confirmed by the local courts of different jurisdictions in the last years, regardless of the legal system adopted by them. Some of these decisions rendered by the highest courts of Switzerland, France, England, and the United States are of particular interest.

The Federal Tribunal of Switzerland has already rendered a decision in favor of the arbitration tribunal, recognizing its competence to decide on its own jurisdiction and on the existence or validity of an arbitration agreement prior to the local courts. The Federal Tribunal held in the *Foundation M.* case, in 1996,[16] that the local court can only intervene when the arbitration agreement is obviously "*null and void, inoperative or incapable of being performed*," without it being necessary to analyze the question in detail.

However, what is interesting about this decision rendered by the Federal Tribunal of Switzerland is that it has limited the court's jurisdiction interference,

[14] *Id.* at 258, 261.
[15] *Id.*
[16] Swiss Fed. Trib., 29 April 1996, *Foundation M.* v. *Banque X.*, ATF 122 III 139, 1996 (3) *ASA Bull.* 527.

when the arbitration agreement is overtly void, if the arbitration tribunal has its seat in Switzerland. The question pending, therefore, is whether the negative effect of Competence-Competence would be recognized when the arbitration tribunal has its seat out of Switzerland and encounters the issue of the validity of the arbitration agreement. There are no precedents facing this matter yet.

In contrast, France has recognized the Competence-Competence principle effects in full, regardless of where the arbitration tribunal has its seat. The French courts have decided in favor of the rule of priority of the arbitrators. Thus, according to French courts, a party who wishes to contest the jurisdiction of an arbitral tribunal cannot seek a ruling from the French courts, because jurisdiction is a matter for the arbitral tribunal to decide in the first instance.

The only obstacle to the Competence-Competence principle is where the arbitration agreement is "*manifestly void*" or "*manifestly not applicable*".[17] With respect to the particular question, the French case law *American Bureau of Shipping*,[18] in which the *Cour de Cassation* held that the overt nullity is the only obstacle to the principle of Competence-Competence deserves attention.[19]

The courts in England, in turn, since the adoption of the 1996 Arbitration Act, have imposed some limitation on the recognition of the negative effect of the principle of Competence-Competence, and, at the same time, empowered the courts to rule on the arbitrators' jurisdiction in relation to the existence, validity and scope of the arbitration agreement.

With respect to the particular question, the House of Lords held in the *Fiona Trust* decision, issued in October 2007,[20] that:

> [The] combination of sections [9 and 72 of the Arbitration Act] shows, together with the prescriptive section 9(4), that it is contemplated by the Act that it will, in general, be right for the arbitrators to be the first tribunal to consider whether they have jurisdiction to determine the dispute. In these circumstances, although it is contemplated also by section 72 that a party who takes no part in arbitration proceedings

[17] Cour de Casssation (Civ. 1ere), October 6, 2010, no. 09-68.731, Blonde Génétique et autre c/ SCEA Plante Moulet et autre, Rev Arb, 2010, pp 971-972; Cour de Cassation (Civ. 1ere), October 16, 2001, Société Quatro Children's Books Limited c/ Société Editions du Seuil et autre, Rev Arb, 2002, p. 920.

[18] Cass, Ie civ., 26 June 2001, *American Bureau of Shipping* (ABS) v. *Copropriété Maritime Jules Verne*, 2001(3) Rev. arb. 529, with note by E. Gaillard; for an English translation, see *Gaillard, E.* (2008). The Negative Effect of Competence-Competence, *Int'l Arb. Rep.*, 27. See also Ibrahim Fadlallah. (2004). Priorité à l'arbitrage: entre quelles parties?, II *Cahiers de l'arbitrage*, 65.

[19] According to Emmanuel Gaillard and Yas Banifatemi, the *Cour de Cassation* held "the manifest nullity of the arbitration agreement to be the only obstacle to the [principle that an arbitrator is entitled to rule on his own competence] that establishes priority of arbitral competence to rule on the existence, the validity and the scope of the arbitration agreement." (In Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. at 263).

[20] *Premium Nafta Products Ltd.* v. *Fili Shipping Co. Ltd.* [2007] UK. Retrieved form https://publications.parliament.uk/pa/ld200607/ldjudgmt/jd071017/ship-1.htm.

> should be entitled in court to 'question whether there is a valid arbitration agreement', the court should, in light of section 1(1) of the Act, be very cautious about agreeing that its process should be so utilized. *If there is* a valid arbitration agreement, proceedings cannot be launched under section 72(l)(a) at all.[21] (emphasis added)

Thus, according to the English court decision, courts remain competent to decide on the existence, validity and scope of the arbitration agreement, if there is a valid arbitration agreement. That is, the arbitrators' jurisdiction is limited by the requirement that a valid arbitration agreement exists, as the courts retain a degree of scrutiny as to the existence, validity and scope of the arbitration agreement. Due to this reasoning of the English courts, Emmanuel Gaillard and Yas Banifatemi states that "*the question of the extent to which English courts will give effect to the negative effect of competence-competence remains uncertain*".[22]

In the United States, the Supreme Court ruled in *First Options, Inc. v. Kaplan* that the arbitration tribunal may decide on a challenge to its jurisdiction as long as there is "*clear and unmistakable evidence*"[23] that the parties intended to submit this question to the tribunal. If there is no clarity regarding to what the parties have decided, the arbitration tribunal may even make a provisional ruling on jurisdiction, however the ruling is reviewable by the national court before an arbitration award has been rendered.

The courts in the United States have consistently applied a presumption in favor of the question of "*arbitrability*", as the court refers to the issue of whether the subject matter of a given claim may be arbitrated, and that includes the question of existence, validity and scope of an arbitration agreement. A recalcitrant respondent cannot bring the proceedings to a halt just by challenging jurisdiction. Proceedings will not be disrupted through a simple allegation that an arbitration clause is unenforceable. It is necessary to be demonstrated that there is no clarity or *unmistakable evidence* that the parties have agreed on delegating the jurisdiction to an arbitration tribunal.

Indeed, certain questions related to the allocation of competence between arbitral tribunals and national courts to decide on the validity of an arbitration agreement remain opened and must be solved. However, although the limitations that remain in certain jurisdictions, as showed above, the rule of priority in favor of arbitrators' recognition has increased.

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21 *Id.* at 34.

22 See Gaillard, E. & Banifatemi, Y. Negative Effect of Competence-Competence: The Rule of Priority in Favour of the Arbitrators. at 268.

23 Graves J. & Davydan Y. (2011). Competence-Competence and Separability – American Style. In *International Arbitration and International Commercial Law: Synergy, Convergence and Evolution.* (p. 161). Touro Law Center.

Towards this direction, Brazil has already recognized the Competence-Competence principle. Over the years, this principle has been accepted by the Brazilian statutory law and it has also driven courts' decision on issues related to arbitrator's jurisdiction. As demonstrated below, the Brazilian legal system has already recognized the applicability of the rule of priority in favor of the arbitrators, which has gained more clarity over the last years. A recent decision rendered by the Brazilian highest court on this matter deserves special attention, as it marks the recognition of the applicability of the Competence-Competence principle upon concession contracts in Brazil.

3 The development of Competence-Competence principle under Brazilian Statutory Law

3.1 Competence-Competence principle codified into Brazilian Statutory Law

It is not from today that the Brazilian legal order provides for the litigants the arbitration as an alternative means of dispute resolution. The history of arbitration in Brazil goes back prior to the formation of the nation, when the disputes arisen between Portugal and Spain regarding the colonization of the lands conquered by them in South America should be solved through arbitration, under the Treaty of Tordesillas.[24]

Since then, several Brazilian statutory laws and even the Federal Constitutions enacted through the time have provided for the parties the possibility to solve their disputes by arbitration.

On September 23, 1996, Brazil enacted the Brazilian Arbitration Act[25] ("BAA"), which provides the proceedings of the arbitration. The BAA was enacted as an attempt to foment the use of arbitration in Brazil, by, mostly, lifting some barriers to the use of the institute which had undermined the adoption of arbitration in Brazil. One of the barriers lifted up was the former requirement to homologation homologate at courts arbitration awards rendered by arbitration tribunals having seats in Brazil in order to produce effects as a judicial decision. Since the parties had to submit the arbitration awards rendered by an arbitration tribunal located in Brazil before the national courts, they were invariably dragged on for years due to the congested Brazilian court system.

[24] Cazzaro, K. & Pereira, J. (Jun, 2014). O Instituto da Arbitragem no Brasil e na Espanha: Comparações Legislativas (p. 54). Retrieved from http://seer.upf.br/index.php/rjd/article /viewFile/4830/3257.

[25] Law no. 9.307, of September 23, 1996.

Furthermore, Article 8, sole paragraph, of the BAA embodies the Competence-Competence principle by providing that the arbitral tribunal is entitled to decide on its jurisdiction as well as on the existence, validity, efficacy and scope of the arbitration agreement, in the following terms:

> Article 8. The arbitration clause is autonomous in relation to the agreement in which it is inserted, whereupon the nullity of the agreement does not necessarily implicate the nullity of the arbitration clause.
>
> Sole paragraph. *It is the arbitrator's duty to decide, on his own motion, or at the request of the parties, issues regarding the existence, validity and effectiveness of the arbitration agreement and of the contract that contains the arbitration clause*. (emphasis added)

As of the BAA, several other statutory laws reaffirmed the arbitration as an alternative of dispute resolutions, amongst them the Law no. 8.987/95 (according to the wording given by the Law no. 11.196/05), which relates to the General Concessions and allowances of the public services. (Article 23.) Moreover, the Article 43, X, of the Law no. 9.478, of August 6, 1997, which governs the national politics regarding energy, and the activities related to Oil & Gas exploration, allowed the parties to set before an arbitral tribunal disputes arisen from oilfield concession contracts.

Moreover, it is worth mentioning that in 2001 the Brazil's Supreme Court decided[26] that the arbitration is a constitutional alternative dispute resolution mechanism, in light of Article 5, XXXV, of the Federal Constitution of Brazil, which provides:

> Article 5. All persons are equal before the law, without any distinction whatsoever, Brazilians and foreigners residing in the country being ensured of inviolability of the right to life, to liberty, to equality, to security and to property, on the following terms:
>
> (...)
>
> XXXV – *the law shall not exclude any injury or threat to a right from the consideration of the Judicial Power*; (emphasis added)

It is important to highlight, also, that Brazil became a party of the New York Convention on June 7, 2002,[27] in accordance to the international arbitration practice.

[26] STF, SE no. 5.206, Reporter Judge Sepúveda Pertence, judged in 12.12.2001, published in 4.30.2004. Retrieved December 2, 2017, from http://stf.jus.br/portal/jurisprudencia.

[27] Retrieved December 3, 2017, from http://www.newyorkconvention.org/countries.

As a reflection of the evolution of the arbitration institute in Brazil, the institute has gained sharper contours in the last years. The new Brazilian Civil Procedural Code (Law no. 13.105/15), enacted on March 16, 2015, has brought a new conception of the institute to the national legal order, as it recognized the arbitration as a state's duty, on which lies in the duty to promote and encourage its adoption. Article 3 of the aforementioned statutory law provides as follows:

> Article 3. Neither injury nor threat to a right shall be precluded from judicial examination.
>
> §1. Arbitration is allowed, in accordance with statutory law;
>
> §2. *The State must, whenever possible, encourage the parties to reach a consensual settlement of the dispute*. (emphasis added)

Besides, it is worth mentioning that the Law no. 13.129, of May 26, 2015 has altered the BAA to allow the Public Administration to adopt the arbitration as an alternative means of dispute resolution as well, in order to solve disputes arisen from disposable equity rights. Article 1, paragraphs 1 and 2, of the BAA, sets forth:

> Article 1. Those who are capable of entering into contracts may make use of arbitration to resolve conflicts regarding freely transferable property rights.
>
> §1. *Direct and indirect public administration may use arbitration to resolve conflicts regarding transferable public property rights*.
>
> §2. The competent authority or direct public administration entity that enters into arbitration agreements is the same entity that enters into agreements or transactions. (emphasis added)

Thus, the arbitration is not a new mechanism of alternative dispute resolution within the Brazilian legal order. However, alterations have been made during the time not only to stimulate the practice, but also to provide legal certainty for the parties.

As a reflection of this expectation, in addition to the new Brazilian Civil Procedural Code reaffirming the arbitration as an alternative dispute resolution (Article 3), the alterations on the BAA, by the Law no. 13.129/15, has also brought important innovations to the legal regime, amongst them, by the giving of more relevance to the Competence-Competence principle.

In this sense, the new wording of Article 20 of the BAA states that if a party disagrees to the jurisdiction of an arbitral tribunal, it must state its disagreement on it as soon as possible before the Arbitration Tribunal, as follows:

> Article 20. *The party wishing to raise issues related to the jurisdiction*, suspicion or impediment of an arbitrator or arbitrators, or as to the nullity, invalidity or ineffectiveness of the arbitration agreement, must do so at the first opportunity, after the commencement of the arbitration.
>
> §1. When the challenge of suspicion or impediment is accepted, the arbitrator shall be replaced in accordance with Article 16 of this Law; *and if the lack of jurisdiction of the arbitrator or of the arbitral tribunal, as well as the nullity, invalidity or ineffectiveness of the arbitration agreement is confirmed, the parties shall revert to the Judicial Authority competent to rule on the matter*.
>
> §2. When the challenge is not accepted, the arbitration shall proceed normally, *subject however to review of that decision by the competent Judicial Authority if a lawsuit referred to in Article 33 of this Law is filed*. (emphasis added)

In addition, Articles 31 and 33 of the BAA[28] safeguard the arbitral tribunal power to determine its own jurisdiction postponing the control of such power to the post-award stage. That is to say that the arbitrator has the competence to decide its own jurisdiction at first.

In fact, Brazil has an extensive arbitration legal framework, which in its current stage provides for the parties enough legal certainty as it allows them to seek arbitration (when the contract is provided with an arbitration clause) as an alternative mechanism to solve any dispute arisen from contracts between either private parties or public administration (i.e., issues related to contract concession), as demonstrated further below.

The evolution of the arbitration in Brazil has gained even more clarity over the last years, and the level of legal certainty has increased even more since the Brazilian Superior Court of Justice has recognized the Competence-Competence principle applicability upon concession contracts related to the Oil & Gas exploration.

As demonstrated below, the Brazilian Superior Court of Justice, which is the highest Court to decide issues related to arbitration, has rendered, on October 11, 2017, a landmark decision addressing the Competence-Competence principle applicability (CC no. 139.519-RJ, Petróleo Brasileiro S.A. – Petrobras v. Brazilian National Agency of Petroleum, Natural Gas and Biofuels – ANP), assuring that the competence of the arbitrator to decide whether it has jurisdiction over a case brought before the arbitration court precedes the state's jurisdiction.

[28] Article 31. The arbitral award shall have the same effect on the parties and their successors as a judgement rendered by the Judicial Authority and, if it includes an obligation for payment, it shall constitute an enforceable instrument thereof.

Article 33. The interested party may request to the competent Judicial Authority to declare the arbitral award null in the cases set forth in this law.

The STJ's decision granted to Petrobras a request to recognize the Competence-Competence principle applicability, in a case which involves ANP and the State of Espírito Santo.

The decision attributed particular relevance to the fact that the arbitration clause incorporated institutional rules. And the existence of such provisions confer competence on the arbitral tribunal to rule on jurisdictional objections.

The STJ overturned the lower Federal Court's decision, which had refused the arbitrator's competence to decide on the existence, validity, efficacy and scope of the arbitration agreement. The parties will now proceed to dispute the validity of the arbitration agreement before an arbitral tribunal.

3.2 Remarkable case law: dispute between Petrobras and the Brazilian Oil & Gas Agency (ANP)

3.2.1 The Brazilian Superior Court of Justice's recognition of the applicability of the Competence-Competence principle to concession agreements

As stated above, the Brazilian Superior Court of Justice has rendered a decision[29] addressing the Competence-Competence principle acceptance by the Brazilian legal order, and its applicability to concession contract related to the Oil & Gas sector (CC no. 139.519-RJ, Petróleo Brasileiro S.A. – Petrobras v. Brazilian National Agency of Petroleum, Natural Gas and Biofuels – ANP).

This decision is important because it defines the allocation of competence between arbitral tribunals and national courts to decide on the validity of an arbitration agreement. In this case, as demonstrated below, the STJ decided on the competence of the ICC Brazil based upon a consent provision in a concession contract signed by the parties, despite the existence of a public body interest. This decision confers clarity to the arbitrator competence limits, and, ultimately, provides legal certainty not only for the Oil & Gas sector, but also for foreign investors which aims to do business in any field in Brazil, since they can rely on this decision in case any dispute arises from a contract that establishes an arbitration clause, even if the public administration is one of the parties involved (for instance, in case of arbitration clauses under concession contracts).

[29] STJ's decision (CC no. 139.519/RJ), Retrieved November 11, 2017, from http://www.stj.jus.br/SCON/jurisprudencia/doc.jsp?livre=139519&b=ACOR&p=true&l=10&i=1.

3.2.2 The case

In 1998 ANP and Petrobras, after the best offer of the latter in Brazil's bidding round, signed an administrative contract for the exploration, development and production of oil and gas in several small oil fields, known as *Parque das Baleias*.

The dispute between Petrobras and ANP arose after ANP's administrative decision, issued in 2014, to merge those small fields under Petrobras' concession with other fields awarded to other companies at the same bidding process, in order to create one single oil field (called *Campo de Jubarte*). The reasoning of the administrative decision, which was followed by the enactment of the Resolution RD no. 69/2014, was justified by ANP as a necessary measure to "*substantially increase the public revenues without, however, affecting the economic viability*" of the ongoing concession contracts.[30] In fact, the most meaningful administrative decision's effect would be the increase of the royalties' income from BRL 17.3 Billion to BRL 44 Billion (from approximately US$ 5.3 Billion to US$ 13.5 Billion).[31]

Due to the government's decision to change the concession contract premises sixteen years after its signature, and its refusal to review it, Petrobras requested the establishment of arbitral proceedings against ANP before the International Chamber of Commerce – ICC (file registered as CCI no. 20196/ASM), located in Brazil, seeking to be granted with an award declaring the administrative decision null and void.

Prior to the establishment of the arbitral proceedings, Petrobras also sought the suspension of the administrative decision, in order to refrain any attempt of the Brazilian Agency to collect any amount greater than that consented by the parties under the concession contract, by requesting an injunction before the Federal Court of the Second Circuit, located in Rio de Janeiro. The injunction requested by Petrobras was promptly granted, however, the Federal Tribunal of the Second Circuit overruled the decision.[32]

In the meantime, ANP filed an anti-suit injunction[33] whereby it sought the suspension of the arbitration proceedings. The ANP's request was, at first, denied by the Lower Federal Court. However, the Federal Tribunal of the Second Circuit granted both ANP and the State of Espírito Santo[34] a request so as to not only to authorize the collection of the amount reported owed by Petrobras, but also to

[30] Pages 7-8 of the records.

[31] On December 4, 2017, the currency rate was US$ 1.00 to BRL 3.25.

[32] Known in Brazil as *Tribunal Regional Federal da Segunda Região*.

[33] As regard the anti-suit injunction, Emmanuel Gaillard states: "*An anti-suit injunction can also prohibit one of the parties from continuing arbitration proceedings that it deems to have been initiated in the absence of a valid arbitration agreement.*" (Gaillard, E. (2005) Anti-suit Injunctions in International Arbitration, 2, 82.)

[34] The State of Espírito Santo appealed against the lower court's refusal to authorize his interference in the lawsuit as interested third party.

recognize the competence of the court to decide the merits of the case, despite the existence of an arbitration clause on the concession contract. According to the Federal Court, the case could not be solved by an arbitral tribunal because it involves public equity rights (known as non-disposable), and, therefore, only a national court would be authorized to decide its merits.

Thereafter, the Arbitral Tribunal ("ICC"), which was running in parallel with the court proceedings, rendered a decision in the opposite way, recognizing its own competence to decide the issue which had arisen and, in consequence, it suspended the effects of ANP's administrative decision, halting any collection based on it.

Because of the existence of two conflicting decisions regarding the same matter, Petrobras filed a motion before STJ, which is the highest competent court to rule on arbitration related matters under Brazil's Federal Constitution, requesting for the recognition of the prevalence of the arbitration clause, and thus of the arbitrators' decision.

According to Petrobras, the arbitration decision should prevail because the arbitral tribunal has the competence to decide its own jurisdiction prior to the national court, even if the case involves a non-disposable equity right. In other words, since there is an arbitration clause in the contract, the Competence-Competence principle should be applied, and hence the competence of the arbitrator to decide whether it has jurisdiction over a case brought before the arbitration court precedes the state jurisdiction.

Conversely, ANP alleged that the Competence-Competence principle would not be applicable to the case, as the issue in question relates to non-disposable equity rights. ANP advocated that only a national court would have jurisdiction to decide the merits of the case since there is public interest involved. Furthermore, ANP contended that, once there is a direct interest of the State of Espírito Santo upon the allocation of the royalties related to the exploration of the fields, and it is not a party of the concession contract, the arbitration clause cannot be imposed over it. Under ANP's reasoning, an arbitration clause can be only imposed upon the contract parties, which have consciously agreed on the establishment of the arbitration clause. Finally, ANP singled out that the acceptance of the Petrobras standpoint would otherwise curtail the State of Espírito Santo's defense.

The reported Judge Napoleão Nunes Maia Filho, at first, granted the injunction requested by Petrobras on the CC no. 139.519-RJ, determining the suspension of all the judicial and administrative proceedings filed against Petrobras, including the anti-suit injunction filed by ANP. Besides, the reported Judge temporarily appointed the ICC Brazil as the only competent jurisdiction to decide the matters related to the case.

However, as demonstrated below, the reported Judge Napoleão Nunes Maia Filho, when deciding the merits of the motion filed by Petrobras, decided in the opposite direction, being followed only by one of the judges of the Panel. The Panel's majority, led by Judge Regina Helena Costa's opinion, granted Petrobras' request, as further demonstrated.

3.2.3 The STJ's decision

The STJ's decision is landmark from the legal certainty standpoint. The majority of the Tribunal[35] followed Judge Regina Helena Costa's opinion, stating that, since there is an arbitration clause indicating ICC Brazil as the competent tribunal to resolve contract disputes, ICC arbitrators must be the *first* judges of their own jurisdiction. In other words, the court's power is postponed until such time as the arbitrators themselves have had the opportunity to render a decision regarding existence, validity and efficacy of the arbitration agreement.

The Tribunal held, in sum, that (i) the Brazilian legal order, including those laws which govern the rules of the Oil and Gas sector, provides for arbitrator competence to decide whether it has jurisdiction over a case brought before the arbitration court or not, *prior to any judicial body*, and (ii) the arbitration clause mutually agreed by the parties should prevail, even if there is a public third party interest involved.

The Tribunal affirmed that Articles 8, 20 and 33 of the BAA (whose writin was altered by the Law no. 13.129, of May, 26, 2015) rule that the arbitrator competence to decide on issues related to existence, validity and effectiveness of the arbitration clause precedes any judicial body, in the following terms:

> This is because it reveals the need for observance of Articles 8 and 20 of Law no. 9.307/96, which confer on the arbitral tribunal the measure of minimum competence, based on the principle of competence and competence, and it is then incumbent upon it to deliberate on the limits of its attributions, previously to any other judicial body, as well as on matters relating to the existence, validity and effectiveness of the arbitration agreement and the contract containing the arbitration clause:[36]

Regarding the ANP defense that, despite the existence of the arbitration clause, the Resolution no. 64/2014 rules that any issue relating to a concession contract cannot be decided by an arbitrator due to the existence of a non-disposable

[35] Judge Regina Helena Costa's opinion was followed by Judge Assusete Magalhães, Judge Mauro Campbell Marques, Judge Sergio Kukina, and Judge Gurgel de Faria.

[36] Pages 1638-1664 of the record.

equity right, and thus of a public interest, the Tribunal rejected ANP's allegation and affirmed that the arbitration clause must prevail. What is interesting regarding this issue is that the Brazilian Agency invoked the unilateral alteration made by itself through a resolution in 2014 in order to set forth the competence of the state to decide about disputes arising from concession contracts.

Also, the Tribunal in this regard singles out that, even though there is a public interest surrounding the case, the issue is not related to non-disposable equity rights. According to the Tribunal's reasoning, not all public equity rights are non-disposable. In the case, since the government has allowed a private party, under a concession contract, to explore a public equity (i.e., oil and gas fields), the public equity right is therefore disposable. As noted by the Tribunal after an extensive review of several judicial decisions, it is also of the public interest to dispose of these equity rights for the exploration of the national mineral resource. In sum, what defines whether an equity right is or is not disposable is not the existence of a public interest, but whether the equity is subject to an economic valuation.

Moreover, the Tribunal rejected the ANP's argument that the arbitration model applicable in Brazil follows the American one, which establishes the jurisdiction of the Judiciary Power to appreciate the validity of the arbitration clause and other related issues (in light of Article II.3 of the 1958 New York Convention). The ANP based its argument on the decree enacted in 2002 in Brazil (Decree no. 4.311, of July 23, 2002), in which Article 3 established that the national court had the jurisdiction to decide on the validity of an arbitration clause. The said decree, in which contained arbitration guidelines in light of the American system, was enacted at the time by virtue of the signature of the New York Convention by the Brazilian government.

However, the STJ highlighted that the abovementioned decree was derogated by the alterations on BAA made by the Law no. 13.129/2015. As the new wording of the BAA recognized, as of 2015, the Competence-Competence principle applicability, the decree disposition is no longer valid. Thus, the STJ's assertion solved the controversy over the rule that shall be applied upon issues related to the allocation of the competence between the arbitral tribunal and the national court by recognizing that the BAA dispositions were no longer effective.

Finally, the Superior Court asserted that, although the State of Espírito Santo is a third party of the concession contract, the arbitration clause is *effective* against it, and therefore should be applied. The Superior Court of Justice held that since the State of Espírito Santo is a third party affected by the concession contract, it may intervene in the ongoing arbitration based on its interest related to how the royalties will be allocated in case of unification of the oil and gas fields. The Tribunal went on to state:

> In addition, as I have already pointed out, it is possible for third parties not signatories of the agreement to intervene in arbitration.
>
> Given the evolution from the contractual nature to the jurisdiction of the arbitration activity and the removal of the state jurisdiction, it is possible the intervention of the State of Espirito Santo, as interested third party, due to the alleged alteration of the criteria of distribution of royalties.

Hence, the Tribunal concluded that it is possible the intervention of the public third party in an arbitration due to the evolution from the contract nature to the jurisdiction of the arbitration activity and the removal of the state jurisdiction.

The reported judge, however, in his dissenting opinion, reversed the reasoning expressed on its decision by which he had granted Petrobras' injunction request, and considered the Federal Court the only competent to decide the issue at hand.

Firstly, according to the judge assigned to the case, the Competence-Competence principle adopted by the Brazilian legal order follows the American model, rather than the French mocdl, in the following terms:

> The methodology adopted in France establishes that competence must be verified initially by the elected arbitrator, with possible legal control, *a posteriori*, by the Magistrate. In turn, the American model, based on the Prima Paint v. Flood & Conklin Manufacturing Co. (1967) by the Supreme Court of the United States of America, establishes the jurisdiction of the Judiciary to appreciate the validity of the clause and other related issues.

Hence, according to the reported judge, only the national court has jurisdiction to decide regarding the existence, validity and efficacy of the arbitration agreement.

Secondly, following this reasoning, the reported judge affirmed that the understanding related to the Competence-Competence principle has minimum importance in the solution of the case, because the arbitration clause cannot be imposed upon a third party of the contract, and thus cannot avoid the State of Espírito Santo to seek the protection of its rights before the Federal Court. Regarding this matter, the reported judge affirmed:

> Although Law 9.307/96 points to the incidence of the French model in Brazilian territory, the New York Convention-CNI, of which the Federative Republic of Brazil is a signatory (Decree 4.311/2002), establishes guidelines for the adoption of the American system, [...]
>
> The provision of art. II:3 of the CNI, in particular, recognizes that the Judicial Power of the signatory State of the Convention has the prerogative to examine the validity and extent of the arbitration clause, verifying that such agreement is null and void, ineffective or unenforceable. It is not otherwise the case. In effect, by overriding the

> rights of the signatories, by interfering with the Internal State Entities that did not agree to the election of the arbitration, the clause is found to be inapplicable, inoperative and even impracticable.

The reported judge's dissenting opinion was followed by Mr. Justice Benedito Gonçalves, who pointed out that the arbitration clause cannot be imposed upon a third party, especially when it is a public party, which holds a public interest. As asserted by Mr. Justice Benedito Gonçalves, by not allowing the State to defend its interests before the judicial system, the Superior Court would curtail its right to defense.

In conclusion, the STJ's decision is a landmark precedent, as it conferred legal certainty by bringing clarity to the limits of the Competence-Competence principle among the Brazilian legal order, by assuring that the arbitral tribunal, previously appointed by the parties in the arbitration agreement (ICC Brazil, in the case under analysis), has competence to decide whether it has jurisdiction to rule on the existence, validity, efficacy and scope of the arbitration agreement.

Moreover, the recognition that the existence of a public interest related to the concession contract does not exclude the arbitration clause effectiveness, gives more clarity to those investors, mainly foreign investors, willing to invest in Brazil (not limited to the oil and gas sector), as regard the issues and risks involved in an investment.

4 Conclusion

The Competence-Competence principle plays an important role in determining who has jurisdiction to decide disputes related to the validity and applicability of arbitration agreements. The acceptance of the Competence-Competence principle by a specific legal system is taken as a matter of great importance to the international arbitration community.

As analyzed during this study, the New York Convention does not expressly allocate jurisdictional competence with respect to an arbitration agreement as between the arbitral tribunal and the relevant national courts. Legal systems, consequently, implemented the principle of Competence-Competence according to their own national laws. For this reason, the competence of national courts versus arbitral tribunals and its extent may vary depending on the jurisdiction.

The recent decision rendered by the Brazilian Superior Court of Justice in *Petrobras v. ANP* provides legal certainty by ensuring the application of the Competence-Competence over concession contracts, despite the existence of a public interest involved. It is true that the STJ had enforced the principle in previous cases. However, this STJ's decision brought clarity regarding the allocation of the

arbitral tribunal's and national court's power to rule on jurisdictional challenges when a public interest is in dispute.

It is worth pointing out that, unlike common law jurisdictions, the STJ's decision does not bind the lower courts in Brazil. Notwithstanding, as the STJ is the highest competent court to rule on arbitration related matters, its decisions are therefore very persuasive, sharpening the contours of the Competence-Competence principle applicability in Brazil. Thus, in practice, similar disputes regarding the arbitrator's competence to decide its jurisdiction prior to the national court are likely to be interpreted in accordance with the STJ's decision at hand.

In sum, by recognizing the application of the Competence-Competence principle to those concession contracts that set forth the arbitration agreement, the Brazilian Superior Court conferred on the international investors legal certainty over the arbitration agreement applicability in Brazil. Also, the effects that may arise from the short to mid-term, as a result of the proper legal conditions provided, are the enhancement of investments – mainly by foreign investors – not only in the oil and gas sector, but also in all sectors where the public interest is present.

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