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The IBA Guidelines on Conflicts of Interest: Portuguese courts differ

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Arbitration analysis: Duarte G. Henriques (BCH Lawyers) and Marta Boura (Lisbon Law School) discuss two recent decisions from Portuguese administrative courts, which have found the IBA Guidelines on Conflicts of Interest in International Arbitration (the IBA Guidelines) to be inapplicable in domestic arbitrations which had generated challenges to arbitrators. They note that the courts' approach differs from other Portuguese case law and they discuss practical implications for international arbitration practitioners.

Original news:

The judgments cited below are all available (in Portuguese) on the Portuguese courts service website (www.dgsi.pt).

What is the Portuguese legal setting in relation to international standards on the conflicts of interest in arbitration?

As the cases analysed below confirm, the discussion over conflicts of interest in arbitration is as alive as ever in Portugal, and far from settled.

The widespread perception of the crucial importance of this matter leaves no doubts as to the duties of impartiality and independence required from arbitrators. However, the path is not so clear as to the interplay between the IBA Guidelines and the Portuguese legal setting. More acutely, there seems to be no consensus as to whether and, if so, how the "Guidelines" should be received in Portugal.

In fact, the progressive internationalisation of the Portuguese jurisdiction and the Portuguese arbitration community has led to an undeniable confrontation between local traditions and the ambitious phenomenon of cross-border ethical regulation (reflected in international standards such as the IBA Guidelines The reactions in some Portuguese courts evidence that clash, as we will see below.

It is not that the pertinence, relevance or content of the Guidelines should not be accepted in Portugal. To the contrary, in our experience, and considering the existing literature and case law on the subject, we believe it is generally agreed that these international standards are appropriate.

However, that consensus seems to exist only in the context of purely commercial arbitrations. Indeed, the same "mindset" is not as accepted in other contexts, such as arbitrations involving public entities.

Generally speaking, arbitrations involving the Portuguese State and public entities enjoy the assistance of the administrative courts (more specifically the "Administrative Central Court", equivalent to the Court of Appeals, save for the enforcement of the arbitral award and a few other matters), while commercial arbitrations are subject to the jurisdiction of the common courts (Courts of Appeal, save for the enforcement of arbitral awards and a few other matters, submitted to the common courts of first instance).The aforementioned con-

siderations show a divide between purely commercial arbitrations and arbitrations involving public entities. In this situation, we could expect when and where international standards will be upheld: acceptance at the common courts (for commercial arbitrations), and rejection at the administrative courts.

However, the adverse reaction in some recent decisions of the Portuguese administrative courts was so strong that some guidance is warranted, lest a contamination to other courts might occur.

On the other hand, another consideration comes into play when assessing the use of the IBA Guidelines in the Portuguese jurisdiction.

Arguably, the purported incorporation of the IBA Guidelines into a few local codes of ethics might have triggered these adverse reactions against such international standards.

As a matter of fact, when the Lisbon Commercial Arbitration Centre enacted its "Arbitrator's Code of Ethics" in 2014 [Available online at http://centrodearbitragem.pt/images/pdfs/Legislacao_e_Regulamentos/Regulamento_de_Arbitragem/Arbitrators_Code_of_Ethics_2014.pdf] one of the authors of this article expressed a critical view of what could be seen as an "incorporation" of the IBA Guidelines into that code of ethics. The provision at stake (Article 1(3)) reads precisely as follows:

'This Code of Ethics shall be interpreted and integrated, bearing in mind the International Bar Association Guidelines on Conflicts of Interest in International Arbitration.'

To the best of our knowledge, this route is unique in the whole international arbitration setting, with the notable exception of the "Code of Conduct for Arbitrators" of the Kuala Lumpur Regional Centre for Arbitration (See nr. 2.1: "The International Bar Association (IBA) Guidelines on Conflict of Interest will be a point of reference in determining the disclosure requirement and whether an Arbitrator is conflicted". Accessible at https://klrca.org/uploads/imguploadckc691e4fcd34a3f05e49b8eb477d2ec21.PDF).

The exact extent to which the meaning of this wording should be taken is yet to be established.

In any event, this formulation seems to conjure the notion that an incorporation of the IBA Guidelines is underlying those provisions. Indeed, when first looking at that provision, one is quickly tempted to consider the IBA Guidelines as an actual part of the "Code of Ethics".

By the same token, a similar notion may well be prompted when reading the "Code of Ethics": the IBA Guidelines should be mathematically applied, as if to deploy a simple binary "true/false" assessment.

Any practitioner or decision-maker well versed in the matters of international arbitration and, more specifically, in the issues arising in the context of conflicts of interests—and that includes the vast majority of Portuguese arbitration practitioners—will readily conclude otherwise. And they will apply the IBA Guidelines as they truly are: pure "guidelines" and not strict mandatory provisions.

Be that as it may, such "mathematical" notions became apparent in the decisions of the administrative courts, as we will see.

What is the latest Portuguese case law in this area?

Two very recent cases decided by the Central Administrative Court South have shown the concerns mentioned above, revealing serious doubts as to the acceptance of the IBA Guidelines in Portugal.

The first one was decided by the Central Administrative Court South, on 30 August 2016, where the arbitrator appointed by the claimant (a private company), holder of a public concession, was challenged by the respondent (a state body) in a dispute over a public concession contract (Central Administrative Court South,

30 August 2016, case ref: 13580/16). The challenge was based on the fact that the arbitrator had been vice-chairman of the general shareholders' meetings' board of the institution bankrolling the holder of the public concession. The Administrative Court denied the challenge request and considered that the IBA Guidelines are a good legal support, yet they are only points of reference. In this sense, "the guidelines are not applicable", and consideration should be given to the dimension of Portugal.

In the second case, the same court developed a much harsher criticism and concluded for the inadequacy of the IBA Guidelines (Central Administrative Court South, 16 February 2017, case ref 20011/16.3BCLSB). In this case, a private entity had brought a claim in arbitration against the Lisbon Municipality and, during the proceedings, it became apparent that the private entity-appointed arbitrator had been chosen by the same company in three prior cases. The problem was not so much that the arbitrator had received those appointments, but more critically that he had not disclosed them before initiating his mandate. The Municipality, accordingly, challenged the arbitrator before the Administrative Central Court South. In the judgment, not only did the Administrative Court dismiss the claim but it also made a frontal attack on the IBA Guidelines which, in its words, would not be the "law of Portugal". In its decision, the Court noted that the rules of Portuguese law are different from the "quasi-law of international private arbitration institutions". For that reason, caution should be taken when applying the IBA Guidelines to "avoid unjustified comparisons and uncritical importations of private foreign theories and usages, *maxime*, those from economies of common law countries".

The Administrative Court also stated that these points of reference should not be taken as mandatory and, for that reason, should not be applied to national arbitration since, given their international character, they would not have the functional aptitude to be applied in a domestic arbitration environment.

This argument was reinforced when the Court refused to go along with a purely mathematica—and, indeed, rigid—application of the Guidelines: "why not [appointments in the] four or five prior years?". All things considered, the Court understood that "two or three" appointments by the same party were an arbitrary standard used to assess the lack of impartiality or independence of "professional arbitration lawyers" who may make their living out of arbitration.

What was the background from previous case law?

The reasoning behind this approach is in great contrast to four other cases where the courts (including the Supreme Court of Justice) relied on the IBA Guidelines as a particularly useful instrument when deciding conflicts of interests, notwithstanding its non-binding nature.

One of the most notable cases was decided by the Lisbon Court of Appeal and related to a challenge against an arbitrator who had been appointed by the same law firm in more than 50 cases in the previous three years (Lisbon Court of Appeal, on 24 March 2015, case ref 1361/14.0YRLSB.L1-1).On that occasion, the Court of Appeal made explicit reference to the IBA Guidelines as a commonly accepted international standard for assessing conflicts of interest and upheld the challenge, as was to be expected.

On a second case, the Portuguese Supreme Court of Justice ruled on an arbitration clause that provided for a unique system of appointment of the arbitral tribunal, composed of five members: two would be the general counsels of both parties, two others would be the chief engineers of both parties, and a fifth being chosen by the four members. The Supreme Court considered such an arbitration clause to be in violation of the duties of independence and impartiality imposed on the arbitrators, also based on the "IBA Guidelines" (Supreme Court of Justice on 12 July 2011, case 170751/08.7YIPRT.L1.S1).

In this second case, there was a clear question of "identity" between the parties and the arbitrators. This particular issue was a replica of a previous case decided by the Oporto Court of Appeal. In that case, one of the arbitrators and the counsel of one of the parties were members of the board of directors of a financial institu-

tion subsidiary of two of the parties in that arbitration (Porto Court of Appeal, on 3 June 2014, case ref. 583/12.2TVPRT.P1).

Finally, the Lisbon Court of Appeal decided a case where the arbitrator had been appointed by the same law firm on a number of other cases related to the same issues in dispute (Lisbon Court of Appeal, on 29 September 2015, case ref 827/15.9YRLSB-1). On that occasion, the Court stressed that:

“Because the arbitrator had not disclosed, at the time of his appointment, his previous participations in identical arbitrations involving the same law firm (…) the violation of such duty to disclose created serious doubts about his independence and impartiality 'in the eyes of Respondent."

These cases share a common ground, as the courts, in all those circumstances, did not shy away from resorting to the IBA Guidelines when assessing the conflicts of interests related to the arbitrators. Indeed, the courts highlighted the relevance of this soft-law instrument as being a useful mechanism that reflects international standards in these matters, and thus provides essential guidance to decide challenges to arbitrators.

How may the Administrative Courts’ decisions be analysed?

The IBA Guidelines do not stem from the self-regulatory pressure of common law countries, and these court decisions fail to show otherwise. In fact, the International Bar Association (IBA) is a private association that brings together lawyers from around the world. It has more than 80,000 members, representing more than 190 bar associations and covering 160 countries, governed by principles of participation and involvement of all its members.

In particular, if we refer to its Guidelines, its Drafting Committee was composed of seven members of common law countries, ten members of civil law jurisdictions and two members of “hybrid” systems (as an example, Canada has aspects of common law in some states and civil law in Quebec). The extended group (“Subcommittee on Conflicts of Interest”) of the Arbitration Commission, counted nine members of common law jurisdictions, seven of “hybrid” systems and fifteen of civil law countries. Moreover, the final product presented is the result of the analysis of rules and case law of several countries, and it is also a reflection of the experience of several specialists in international arbitration.

Therefore, the common law “component” is not preponderant.

Additionally, the goal of the IBA Guidelines was not to establish a binding “common law” framework, but rather to promote a greater level of consistency in the assessment of situations that may entail disclosure requirements.

Finally, the Guidelines are not "legal statutes", nor do they claim to be, so they do not replace legal rules or contractual provisions agreed by the parties.

Therefore, considering its non-legally-binding and non-exhaustive nature, it cannot be claimed that they are intended to apply mathematically.

There are, of course, singular and concrete situations that do not allow much room for doubts in the assessment. This seems to be almost self-evident in the second case abovementioned, where the arbitral panel was composed of a lawyer and a party's representative. Those situations will not require more than an almost automatic and mathematical application of the IBA Guidelines.

The underlying meaning is that the IBA Guidelines must not be construed as a rule but rather as guidance in assessing possible conflicts of interests.

Further, one of the main criteria of the IBA Guidelines is “(…) if facts or circumstances exist, or have arisen since the appointment, which, from the point of view of a reasonable third person having knowledge of the relevant facts and circumstances would give rise to justifiable doubts as to the arbitrator’s impartiality or independence (…)” (Standard 2(b)). This criterion is supplemented with the following:

Doubts are justifiable if a reasonable third person, having knowledge of the relevant facts and circumstances, would reach the conclusion that there is a likelihood that the arbitrator may be influenced by factors other than the merits of the case as presented by the parties in reaching his or her decision. (Standard 2(c)).

Regarding the duty to disclose, the “IBA Guidelines” provide that,

“If facts or circumstances exist that may, in the eyes of the parties, give rise to doubts as to the arbitrator’s impartiality or independence, the arbitrator shall disclose such facts or circumstances to the parties, the arbitration institution or other appointing authority (…)” (Standard 3(a)).

The critical factor here is, therefore, what the parties may think of a situation that only the arbitrator is aware of because it has not been disclosed. This assessment requires from the arbitrator an additional effort to place herself or himself above her or his personal belief and intimate criteria.

Of course, everyone thinks of herself or himself to be above any suspicion. However, that is not the point, as this particular case evidences and the guidelines indicate.

In other words, considering the previous appointments of the arbitrator in question and that he failed to disclose such previous appointments, should a *reasonable third person, having knowledge of the relevant facts and circumstances, reach the conclusion that there is a likelihood that the arbitrator may be influenced by factors other than the merits of the case*? Further, was such risk evident in “the eyes of the parties”?

In light of these considerations, the existence of appointments in two or three previous occasions might well have been irrelevant, and one single appointment could justify those “reasonable doubts”, especially if coupled with the failure to disclose such previous appointments. More to the point, what matters is the existence of “likely” doubts, and this is a question of an “impression” that is created, not of a mathematical judgement.

What are the practical implications?

These decisions also confirm fears already expressed of the "incorporation" of the IBA Guidelines in a “Code of Ethics”, in particular the Code of Ethics of the Arbitrator of the arbitrations submitted to the Arbitration Rules of the Commercial Arbitration Centre of the Portuguese Chamber of Commerce and Industry.

These decisions reveal that at least a part of the Portuguese arbitral community is not yet fully prepared to receive regulatory instruments aimed at establishing criteria that are acceptable and, indeed, accepted in numerous other jurisdictions.

The “IBA Guidelines”, with all their virtue, happen to be mistreated when realising these difficulties.

The argument that such instruments apply only to "international arbitration" should not stand. A conflict of interests—such as those decided by the Administrative Court—and the failure to comply with the disclosure duty have nothing to do with the national or international nature of the dispute.

The option taken—the "incorporation" of the IBA Guidelines into the "Code of Ethics"—was, in our view, questionable. However, the existence and usefulness of the IBA Guidelines are not and cannot be ignored if Portugal still intends to become a hub for international arbitrations.

In sum, this analysis seeks to bring forward what has been felt within Portuguese arbitration. In fact, it is no longer a surprise that the field of arbitration has been understood in such different points of view. While some

traditionalists believe arbitrators are capable of self-regulating their independence, others express concerns about the need to safeguard appearances and assure a degree of oversight by the courts.

The increasing internationalisation will warrant a thoroughgoing paradigm shift, but it cannot prevail without due caution. It is hoped that these episodes and the mindset echoed in those Administrative Court's decisions have no other purpose than to warn of these difficulties, as long as the structured and weighted evolution of Portuguese arbitration depends on it.

What should foreign practitioners take into consideration when dealing with these issues in Portugal?

When it comes to evaluating a potential application of the IBA Guidelines foreign practitioners should start by determining in which general area of the law the question should be asked—administrative or commercial law.

In any event, the greatest concern must be focused on the right appointment of arbitrators who cannot fall under any situation giving rise to a potential conflict of interests, whether applying the IBA Guidelines or any other law.

In the meantime, we can assert that the Portuguese jurisdiction pushes forward not only in paying careful attention to conflicts of interests, but more importantly in seeking to avoid them at any rate. This endeavour is unquestionably an investment that is being undertaken by the Portuguese jurisdiction, and reaching a level where conflicts of interests are invariably checked and avoided is certainly a virtue. We can thus say that Portugal is “investing in virtue”.

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