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Annulled *Commisa v Pemex* arbitration award enforced

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Arbitration analysis: Steven Finizio and Santiago Bejarano of WilmerHale discuss the Court of Appeals for the Second Circuit's decision to allow the enforcement of the award in the *Commisa v Pemex* arbitration, despite it having been annulled in the seat of arbitration.

What was the background to the decision?

In a recent decision, *Corporacion Mexicana de Mantenimiento Integral, S De RL De CV v Pemex-Exploracion y Produccion*, No 13-4022 (2d Cir Aug 2, 2016), the US Court of Appeals for the Second Circuit affirmed a district court decision recognising an arbitral award that had been set aside by a court in Mexico, where the arbitration was seated. In doing so, the court added to a small but growing list of international decisions enforcing annulled awards. At the same time, the court reinforced a restrictive approach to the issue of enforcing annulled awards not seen in decisions by courts from other jurisdictions.

The case has an unusual procedural history. The claimant in the arbitration, *Corporacion Mexicana de Mantenimiento Integral, S De RL De CV* ('Commisa'), a Mexican affiliate of American contractor KBR specialising in public infrastructure projects, obtained an award against the Mexican state-owned oil company, Pemex, in an ICC arbitration seated in Mexico.

Commisa then initiated proceedings in New York to have the award recognised, so that it could seek recovery against Pemex's assets in the US. After the US District Court for the Southern District of New York recognised the award, Pemex moved to vacate that judgment on the basis that the award had been set aside by a Mexican court. Because the award had been annulled, the US Court of Appeals ordered that the judgment be vacated, and remanded the case to the district court for further proceedings.

After further proceedings, the district court again confirmed the award, finding that it should not give deference to the Mexican court's decision to annul the award because it violated fundamental principles of due process and justice, and left Commisa without a forum to hear its claim. *Corporacion Mexicana de Mantenimiento Integral, S De RL De CV v Pemex-Exploracion y Produccion*, 962 F Supp 2d 642

Pemex appealed that decision, but the Court of Appeals affirmed the district court's decision to confirm the award despite its annulment in Mexico.

Why is the decision significant?

The *Commisa* case is the second decision in which a US court has recognised an arbitral award that has been annulled in the seat of arbitration. The Court of Appeals' decision reinforces previous case law recognising that the language of art V of the New York Convention (and art 5 of the applicable inter-American Panama Convention (see below)) is discretionary, rather than mandatory. In doing so, a significant US court—the Second Circuit Court of Appeals, which has jurisdiction over New York, among other places—has joined a number of courts in other countries that have also held that they have the authority to recognise foreign arbitral awards that have been annulled at the seat, although these courts differ on the appropriate standard for exercising that authority.

The US court's approach contrasts, for example, with the French approach, where courts have held that they have absolute authority to recognise an annulled award and give no deference to the decision of the foreign court annulling the award. The Cour d'Appel in Paris explained in its well-known decision in *The Arab Republic of Egypt v Chromalloy Aeroservices Inc.*, recognising an award that had been made and annulled in

Egypt, that an international award 'is not integrated in the legal order of that State so that its existence remains established despite its being annulled and its recognition in France is not in violation of international public policy.'

In contrast to the French approach, in *Commisa* the Second Circuit articulated a standard that sets a high bar for enforcing annulled awards: the court's approach precludes a court from exercising its authority to enforce an annulled award unless there is an 'adequate reason' to do so. In particular, the court's approach appears to require a showing that the decision setting aside the award in the seat of arbitration is contrary to US public policy. While the court acknowledged that this requirement is not expressly found in the New York or Panama Conventions, it nonetheless concluded that it is required by the principle of comity.

Given the stringent standard articulated by the Second Circuit, and the general US approach which has been to consider the principle of comity in analysing this question, it remains likely that US courts will only rarely exercise the discretion to enforce foreign arbitral awards that have been annulled in the seat of arbitration. This is certainly the approach in the Second Circuit and in the DC Circuit, following *Baker Marine* (see below) and this recent decision in *Commisa*.

What were the relevant facts?

Commisa entered into a contract with Pemex to build a series of offshore gas platforms in the Gulf of Mexico. When a dispute arose, *Commisa* initiated an ICC arbitration seated in Mexico City and governed by Mexican law, for breach of contract. After *Commisa* commenced the arbitration, Pemex purported to rescind the contract. *Commisa* then sought to challenge the rescission in local courts, and when those efforts failed, it sought damages for wrongful termination in the pending arbitration. The arbitral tribunal found Pemex liable for the wrongful termination of the contract and ordered Pemex to pay *Commisa* \$300m dollars in damages. Notably, during the arbitration, the tribunal issued an interim award finding that it had jurisdiction to hear the case. Pemex did not challenge that decision or raise the issue of arbitrability, even though Mexican law allowed for the interim award to be appealed.

Commisa then sought to have the award recognised in the US by filing an action in the district court in New York (the award was a foreign award for purposes of recognition and enforcement in the US because it was made in Mexico). Pemex opposed recognition in the New York court and simultaneously filed an action in Mexico to set aside the award.

The district court in New York confirmed the award, while the Mexican court rejected Pemex's request to vacate the award. Pemex subsequently filed a constitutional action (*amparo*) in Mexico seeking to vacate the award on constitutional grounds. It did not succeed in the first instance but, on appeal, the Eleventh Collegiate Court in Mexico found for *Commisa* and vacated the award.

The Mexican court of appeals vacated the award on the ground that it addressed matters that were not arbitrable. The court held that, because the arbitration was filed against an entity of the Mexican government, and addressed administrative law issues, the administrative courts had exclusive jurisdiction to hear the matter. In particular, the court concluded that Pemex's rescission of the contract was a governmental action that was not subject to arbitration. In reaching this conclusion, the court also relied on the recently enacted Law of Public Works and Related Services (which was not in force at the time the contract was executed or rescinded) as evidence that the dispute was not subject to arbitration. Section 98 of that statute prohibits submitting disputes arising out of an administrative rescission to arbitration.

What did the US District Court decide?

The question faced by the district court on remand from the US Court of Appeals—whether it could and should confirm the award despite the fact that it had been set aside by a court at the seat of arbitration—arose in the context of the Inter-American Convention on International Commercial Arbitration, also known as the Panama Convention, which applies between the members of the Organisation of American States (OAS). Similar to the New York Convention, the Panama Convention provides for the recognition and enforcement of arbitration agreements and foreign arbitral awards in the courts of its signatories.

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The relevant language in art 5(1) of the Panama Convention (and art V(1) of the New York Convention) provides that a court ‘may’ refuse to recognise and enforce an award in the limited set of circumstances set forth in that article. The district court noted that the word ‘may’ provides discretion to refuse recognition and enforcement exclusively in those circumstances and that it was otherwise bound to recognise a foreign arbitral award under the US Federal Arbitration Act, which implements the Panama Convention.

The court also recognised that the use of the word ‘may’ meant it had discretion to recognise and enforce an award even if it had been annulled in the seat of arbitration. In considering the scope of that discretion, the district court reviewed earlier decisions from the US Court of Appeals for the Second Circuit in *Baker Marine (Nig) Ltd v Chevron (Nig) Ltd*, 191 F 3d 194 (2d Cir 1999) and the US Court of Appeals for the DC Circuit in *TermoRio SA ESP v Electranta*, 487 F 3d 928 (DC Cir 2007).

In both cases, the courts of appeals had refused to recognise arbitral awards that had been annulled at the seat of arbitration on the basis of judicial comity, which requires US courts to give deference to foreign courts’ judgments and recognise them. In *Baker Marine*, the Second Circuit found that there was not ‘adequate reason’ that justified not giving comity to the foreign court’s judgment annulling the award in that case. Similarly, in *TermoRio*, the DC Circuit held that the principle of comity meant that an annulled award could only be recognised where the foreign judgment vacating the award violates basic notions of justice accepted in the US.

In addition to those two cases, the district court also considered the decision in *Chromalloy Aerospacevices, A Division of Chromalloy Gas Turbine Corp v Arab Republic of Egypt*, 939 F.Supp. 907 (DDC 1996), in which a district court in Washington, DC had enforced an award that had been annulled in the seat of arbitration. In that case, the court found that the decision of the Egyptian court to annul the award was contrary to the parties’ express waiver of the right to appeal the award, and that refusing to enforce the award in that circumstance was contrary to US policy in favor of enforcing arbitration clauses.

The district court acknowledged that the *Chromalloy* decision had been criticised as overly broad, but found that all three cases supported the conclusion that art V of the New York Convention (and, therefore, art 5 of the Panama Convention) gave it the authority to enforce an annulled award where failure to do so would violate basic notions of justice.

In considering the Mexican annulment decision, the district court found that there were compelling reasons for it to exercise its discretion under art 5 of the Panama Convention and to confirm the award:

First, the district court considered that the Mexican court of appeals had relied primarily on Section 98 of the Law of Public Works and Related Services, and that it was therefore retroactively applying a law to events that had occurred before it had been enacted. It also found that, at the time the contract was concluded, Commisa had no reason to believe that an eventual dispute arising out of the contract, including matters involving its termination, would not be arbitrable because the enabling statute that created Pemex expressly permitted it to agree to arbitrate its disputes, without placing any limit on the scope of the arbitration agreements it could enter into.

Second, it noted that the Mexican courts with exclusive jurisdiction to hear administrative law claims had refused to hear Commisa’s claim (because the 45-day period for bringing such claims had run). The exclusive jurisdiction of these courts and the short statute of limitations had been established under a law enacted after the contract was executed and subsequently rescinded. The district court therefore found that the decision annulling the award on the grounds that it was non-arbitrable meant that Commisa effectively had no forum where its claim could be heard.

Based on these considerations, the district court distinguished the circumstances from those in the *Baker Marine* and *TermoRio* decisions, and concluded that this case raised issues of fundamental fairness and

public policy that justified exercising its authority under the Panama Convention to recognise a foreign arbitral award that had been annulled in the seat of arbitration.

What did the US Court of Appeals decide?

In addressing whether the district court had the authority to recognise an annulled award and, if so, whether it had properly exercised that authority, the Court of Appeals first considered the general principle that arbitration awards issued in a foreign jurisdiction should be enforced as a matter of public policy. It agreed with the district court that the language ('may') in art 5 of the Panama Convention gave the court discretion to recognise an annulled award.

It then considered the question of the scope of a court's discretion under art 5. The Court of Appeals found that its 'discretion is constrained by the prudential concern of international comity, which remains vital notwithstanding that it is not expressly codified in the Panama Convention.' In addition, the court reiterated the general principle that a foreign judgment is generally conclusive, unless enforcement would offend the public policy of the state in which enforcement is sought.

After laying out these general principles, the Court of Appeals concluded that the district court had not abused its discretion in recognising the award. The court based its decision on four main considerations.

First, it found that Pemex had waived any jurisdictional argument based on questions of arbitrability by failing to challenge the interim award in which the arbitrators decided they had jurisdiction to hear the case.

Second, it found that the Mexican court of appeals retroactive application of the new law was 'repugnant to United States law,' and unfair. The court reasoned that, not only had the Mexican decision applied legislation that was not in effect at the time the contract was entered into, but that there was no other statute or law that otherwise precluded the arbitrability of the type of claim involved.

Third, it found that refusing recognition would leave Commisa without a forum, and that was contrary to the 'imperative of having cases heard—somewhere.' In the court's view, this magnified its concerns about the fairness of the Mexican court's decision.

Fourth, the court found that the annulment had 'frustrated relief that had been granted to COMMISA in the arbitral forum' and left Commisa without a forum, which 'amounted to a taking of private property without compensation for the benefit of the Government.' The court considered that 'in the United States, this would be an unconstitutional taking... [a] feature of United States law [that] is not peculiar to this country.'

On that basis, the Court of Appeals affirmed the district court's decision that it was appropriate to exercise the discretion granted by art 5(1)(e) of the Panama Convention (and, by analogy, art V(1)(e) of the New York Convention) to recognise the annulled award.