PEMEX and US Enforcement of Foreign Arbitration Awards Nullified in Their 'Home' Courts

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One of the benefits of using arbitration to resolve international disputes is the availability of worldwide mechanisms to enforce an arbitral award. For example, the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) and the 1975 Inter-American Convention on International Commercial Arbitration (Panama Convention) state that a "winning" party may take an award rendered in a signatory country and enforce it in the courts of any other signatory country where the losing party's assets are located. Moreover, these treaties provide only very narrow grounds upon which a court may refuse enforcement of a foreign award. Such grounds include violation of fundamental due process, the absence of an arbitration agreement or a breach of international public policy.

The New York Convention also empowers a court to decline enforcement of an award that had been "set aside ... by a competent authority of the country in which, or under the law of which, that award was made." The Panama Convention has a similar provision. A "set aside" sometimes occurs where the "losing" party resided in the country where the award was made and/or was affiliated with that country's government and persuaded its own local courts to annul the award, leading to claims that it used its "home court advantage."

Historically, the attitude of U.S. courts toward foreign set-aside decisions has varied. Several courts have taken the view that, where an award was annulled in the place where arbitration occurred, the award can no longer be enforced in the United States. A few U.S. decisions have taken a different view. In 2016, in *COMMISA v. PEMEX*, the U.S. Court of Appeals for the Second Circuit held that, under the right circumstances, U.S. courts may enforce international arbitration awards even when foreign jurisdictions annul them.

Enforcement in US Courts

PEMEX arose from a dispute between private enterprise COMMISA, a Mexican subsidiary of the Texas-based corporation KBR Inc., and state-owned Mexican petroleum company PEMEX concerning two contracts to build oil platforms in the Gulf of Mexico. Those contracts provided for arbitration of disputes in Mexico. In 2009, an arbitral tribunal awarded COMMISA over $350 million in damages for breach of the construction contracts. In 2011, however, a Mexican court set aside the award, on the grounds that Mexican administrative law did not permit arbitration of claims against a state instrumentality.

Undeterred, COMMISA sought enforcement of the award in U.S. courts. In 2013, a New York federal judge held that the award should be enforced because the Mexican court judgment had offended "basic notions of justice" by retroactively applying administrative laws in such a manner that rendered the case nonarbitrable. The Second Circuit affirmed the lower court's decision on August 2, 2016.

The Second Circuit's ruling is in sharp contrast with previous rulings on the issue, including in *TermoRio S.A. E.S.P. v. Electranta S.P.* (D.C. Cir. 2007), in which the U.S. Court of Appeals for the District of Columbia Circuit held that, absent "extraordinary circumstances," awards that were set aside by the courts of the country in which they were made should not be enforced in the United States. That case involved annulment by the Colombian courts of an international arbitration award rendered in that country.

Several recent U.S. decisions have followed the *TermoRio* approach. In *Thai-Lao Lignite (Thailand) Co. v. Gov't of Lao People's Democratic Rep.* (S.D.N.Y. 2014), a New York federal court denied enforcement of an arbitration award rendered in Kuala Lumpur that was subsequently set aside by Malaysian courts. And in *Getma Int'l v. Rep. of Guinea* (June 9, 2016), the U.S. District Court for the District of Columbia denied enforcement of an award rendered by a regional West African arbitral tribunal that had been set aside by Ivory Coast courts on the grounds that the arbitrators allegedly were paid above ordinary scale.

In *PEMEX*, the Second Circuit held that under the Panama Convention's enforcement framework, a U.S. court "*must* enforce an arbitral award rendered abroad unless a litigant satisfies one of the seven enumerated defenses [in Article V of the Convention]; if one of the defenses is established, the district court *may* choose to refuse recognition of the award" (emphasis in original). Here, one of those defenses was established, *prima facie*, because the award had been set aside in the courts of the place in which it was made.

Although the Panama Convention provided "discretion" as to whether to give effect to the Mexican court's ruling, the Second Circuit held that this discretion "is constrained by the prudential concern of international comity," which treats the judgment of a foreign court as conclusive "*unless* ... the enforcement of the foreign judgment would offend the public policy of the state in which enforcement is sought — which requires the US court to analyze whether the foreign set-aside decision violated fundamental notions of what is decent and what is just" (citation and internal quotations omitted; emphasis in original).

The Second Circuit held that the Mexican court's decision in setting aside the award violated these principles. In particular, it found that: (1) the Mexican court had allowed an "eleventh hour" sovereign immunity defense to succeed, even though PEMEX had not timely raised this defense during the arbitration; this "shattered" COMMISA's "investment-backed expectation in contracting" and "impair[ed]" a "core" precept of contract law; (2) the Mexican court's decision allowed Mexico's statutes to be enforced on a "retroactive" basis so as to shield PEMEX from arbitration; (3) the set-aside decision deprived COMMISA of any effective forum for seeking relief; and (4) the net effect of the decision was to expropriate assets, without compensation. Thus, the lower court's decision affirming the award, and entering judgment against PEMEX, was affirmed.

In reaching its conclusion, the Second Circuit panel wrote that a court should "act with trepidation and reluctance in enforcing an award that has been declared a nullity by the courts having jurisdiction over the forum in which the award was rendered." However, it concluded that the *PEMEX* case was not one of the U.S. courts "second-guess[ing]" a foreign judicial decision. Rather, in this "rare" case, enforcement of the foreign award was necessary to uphold "public confidence in laws" and to prevent the diminishment of "personal rights and liberty."

PEMEX, having failed to obtain *en banc* review of the Second Circuit's decision, will likely seek to appeal the matter to the U.S. Supreme Court. Regardless of whether the Court weighs in on the issue, *PEMEX* is not likely to be the last case to deal with awards that are vacated in the losing party's "home" court — and the U.S. courts are not the only courts to have addressed this issue. For example, in 2016, the French courts held that a large arbitration award against Russia (brought by the former shareholders of Yukos) may be enforced, even though it was annulled by a first-instance judge in the Netherlands, where the arbitration occurred.

These cases thus serve as a timely reminder not only of the importance of choosing an appropriate arbitration seat but also of the complex enforcement issues that may arise once an award is rendered. They also show that, although the U.S. courts generally will respect the decisions of foreign courts (such as those in Mexico), that deference is far from absolute, and foreign judicial decisions will not be enforced where they violate basic U.S. conceptions of fairness and due process.