ALERT MEMORANDUM

Second Circuit Confirms That an Arbitral Award That Has Been Nullified at the Seat of the Arbitration Should Rarely Be Enforced

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On July 20, 2017, in *Thai-Lao Lignite (Thailand) Co., Ltd. v. Gov't of the Lao People's Democratic Republic*, the Second Circuit upheld a district court decision vacating its prior enforcement of a $57 million arbitral award against Laos after the award was annulled by a court at the seat of the arbitration.

In its most recent notable decision on the subject, *Corporación Mexicana de Mantenimiento Integral, S. de R.L. de C.V. v. Pemex-Exploración y Producción*, the Second Circuit had confirmed that U.S. courts asked to enforce nullified arbitral awards should defer to the decisions of courts in the primary jurisdiction absent a violation of "'fundamental notions of what is decent and just' in the United States,"[1] but the Court had applied this standard in a way that many found controversial.

Thai-Lao Lignite returns the Court to a more deferential application of the standard, which promotes the pro-arbitration and international comity principles embodied in the New York Convention. The decision further ensures that these principles will be vindicated even when an arbitral award has already been recognized and enforced in the United States, but later annulled at the seat of the arbitration.

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[1] 832 F.3d 92, 107 (2d Cir. 2016), cert. dismissed, 137 S. Ct. 1622 (2017) ("*Pemex*") (quoting *TermoRio S.A. E.S.P. v. Electranta SP.*, 487 F.3d 928, 938 (D.C. Cir. 2007)).

Enforcing Annulled Awards

When an arbitral award is annulled at the seat of the arbitration (the primary jurisdiction), the party that originally prevailed may nonetheless seek to enforce the award in another jurisdiction (the secondary jurisdiction). Courts in the secondary jurisdiction must then determine how to treat the judgment of the court that nullified the award.

Article III of the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention"), which has been ratified by 157 countries, requires the courts of signatory states to recognize and enforce foreign arbitral awards in accordance with the conditions set forth in the Convention. However, Article V provides that recognition and enforcement of an award "may be refused, at the request of the party against whom it is invoked," in certain enumerated circumstances, including when the award "has been set aside by a competent authority of the country in which, or under the law of which, that award was made."

U.S. courts confronted with actions seeking to enforce awards annulled at the seat of the arbitration have consistently accorded substantial deference to courts in the primary jurisdiction. They have done so with two primary objectives: (1) ensuring a predictable and efficient framework for parties who choose to resolve their disputes through arbitration, and (2) promoting respect and cooperation between the United States and foreign jurisdictions by upholding foreign judgments unless doing so would offend U.S. public policy.

In its first decision on the issue in 1999, *Baker Marine (Nig.) Ltd. v. Chevron (Nig.) Ltd.*, the Second Circuit upheld the district court's refusal to enforce an award that had been annulled in Nigeria, the seat of the arbitration.[2] The Court recognized that second-guessing the primary jurisdiction would "seriously undermine finality" of arbitral proceedings and "regularly produce conflicting judgments."[3] This, in turn, would give a losing party "every reason to pursue its adversary with enforcement actions from country to country until a court is found, if any, which grants the enforcement."[4]

Eight years later, in *TermoRio S.A. E.S.P. v. Electranta S.P.*, the D.C. Circuit also affirmed a decision denying enforcement of an annulled award, stressing not only the risk to the international arbitration framework, but also to international comity.[5] The *TermoRio* court ultimately concluded that "when a competent foreign court has nullified a foreign arbitration award, United States courts should not go behind that decision absent extraordinary circumstances," which are only present when the judgment is "'repugnant to fundamental notions of what is decent and just'" in the United States.[6]

The *Pemex* Decision

The Second Circuit revisited this issue last year in *Pemex*, where it considered whether to enforce an arbitral award that had been set aside by a Mexican appellate court. While the *Pemex* panel confirmed the standard set out in *Baker Marine* and *TermoRio*, recognizing that "[a]ny court should act with trepidation and reluctance in enforcing an arbitral award that has been declared a nullity by the courts having jurisdiction over the forum in which the award was rendered,"[7] it nonetheless became one of the only U.S. courts

[2] 191 F.3d 194, 196 (2d Cir. 1999).
[3] *Id.* at 197 n.3.
[4] *Id.*
[5] 487 F.3d 928 (D.C. Cir. 2007)
[6] *Id.* at 938 (quoting *Ackermann v. Levine*, 788 F.2d 830, 837 (2d Cir. 1986)).
[7] *Pemex*, 832 F.3d at 111.

ever to enforce an award annulled in the primary jurisdiction.

Its decision to do so in light of the record in the case was controversial. The Second Circuit panel concluded that the Mexican appellate court had retroactively applied Mexican law and deprived the plaintiff of a remedy, contrary to fundamental U.S. public policy.[8] Yet it appeared not to have been presented with evidence that would call into question the independence or impartiality of the Mexican court, which it recognized was the equivalent of the D.C. Circuit Court of Appeals.[9] In addition, the Mexican court itself apparently had explained that it had not applied substantive legislation retroactively, but had clarified an open issue under Mexican law using recent legislation as a guiding principle.[10]

The *Pemex* decision raised concerns that U.S. courts might in fact be willing to second-guess foreign annullment judgments they consider ill-reasoned or unfair, despite the stringent standard established in *Baker Marine* and *TermoRio* to protect finality, efficiency, and international comity.

The *Thai-Lao Lignite* Case

Thai-Lao Lignite was originally brought by Thai-Lao Lignite Thailand Co. Ltd. and its subsidiary Hongsa Lignite Lao PDR Co. Ltd. The petitioners asked the district court to enforce an arbitral award rendered in Malaysia against the government of the Lao People's Democratic Republic in connection with Laos' termination of contracts granting the petitioners the right to mine lignite and build a lignite-burning power plant in Laos. While Judge Kimba M. Wood initially issued an enforcement order, the arbitral award was subsequently annulled by the Malaysian High Court based on a finding that the arbitral panel had exceeded its jurisdiction by addressing disputes under contracts not covered by the relevant arbitration agreement.

Laos then moved under Federal Rule of Civil Procedure 60(b)(5) to vacate the district court's judgment enforcing the award. Judge Wood granted this motion, finding that the Malaysian High Court's decision to set aside the award on a "universally recognized ground" did not meet the "'extraordinary circumstances' envisioned by *TermoRio*" and vacating her prior enforcement order.[11] The petitioners appealed this decision to the Second Circuit.

The Second Circuit's Decision

The Second Circuit panel in *Thai-Lao Lignite* concluded that Judge Wood did not abuse her discretion in vacating her earlier judgment enforcing the arbitral award in light of its annulment by the Malaysian High Court. It once again reiterated the high standard for enforcing a nullified award set out in *Baker Marine* and *TermoRio*, and cited *Pemex* primarily to note that it too "recognized a strong presumption in favor of following the primary jurisdiction's ruling."[12]

Although the *Thai-Lao Lignite* panel recognized the need to determine how this presumption applied in the unique procedural posture of the case before it, the panel did not hesitate to find that Rule 60(b)(5) applies to

[8] *Pemex*, 832 F.3d at 108-10.
[9] *See id.* at 99.
[10] *See* Joint Appendix, Volume 13 of 14, *Corporación Mexicana de Mantenimiento Integral, S. de R.L. de C.V. v. Pemex-Exploración y Producción*, No. 13-4022 (2d Cir. Jan. 28, 2014), Dkt. No. 54, at A3763 (Certified English Translation of September 21, 2011 Decision of Eleventh Collegiate Court of Mexico).
[11] *Thai-Lao Lignite (Thailand) Co., Ltd. v. Government of the Lao People's Democratic Republic*, 997 F. Supp. 2d 214, 223, 227 (S.D.N.Y. 2014).
[12] *Thai-Lao Lignite (Thailand) Co., Ltd. v. Government of the Lao People's Democratic Republic*, Case No. 14-597(L), 2017 WL 3081817, at *8 (2d Cir. July 20, 2017).

district court orders enforcing foreign arbitral awards under the New York Convention. The panel further held that "annulment of an arbitral award in the primary jurisdiction should therefore be given significant weight" in the Rule 60(b)(5) analysis,[13] especially in the circumstances of the case at hand, where "although we might not necessarily agree with the merits of the Malaysian courts' judgments, we see no grounds for [public policy] concerns."[14]

Nonetheless, the panel also recognized that courts "should be guided by the full range of interests protected by Rule 60(b)," including "whether the motion was made within a reasonable time, whether the movant acted equitably, and whether vacatur would strike an appropriate balance between serving the ends of justice and preserving the finality of judgments."[15]

The panel found that the district court had at least implicitly considered and permissibly resolved these issues. Although Laos allegedly engaged in a range of inequitable conduct, including delaying moving to setting aside the award in Malaysia and failing to timely comply with the district court's discovery orders, the panel noted that the district court had already denied sanctions against Laos and likely "would not have viewed the conduct as sufficiently dilatory to justify its continued enforcement of an annulled award."[16] Indeed, the panel pointed out, "to rule that the conduct entirely precluded the requested vacatur under Rule 60(b)(5), would mean in effect directing the District Court to enter the equivalent of a $57 million sanction against Laos for its misconduct—a steep fine indeed."[17]

In light of all of these factors, the panel concluded, Judge Wood did not exceed the permissible bounds of her discretion by vacating her prior judgment.

The Path Forward

The Second Circuit's decision in *Thai-Lao Lignite* ensures that even when courts enforce arbitral awards despite pending annulment proceedings abroad, those enforcement orders may successfully be challenged if the award is ultimately set aside. This should provide a certain degree of comfort to award debtors with assets in the United States, though it may also lead to a lengthier enforcement process overall, increasing uncertainty for debtors and creditors.

More significantly, however, the Second Circuit's decision should provide significant reassurance to those concerned about the potential negative ramifications of *Pemex*. *Thai-Lao Lignite* strongly endorses the pro-arbitration and international comity principles embodied in the New York Convention by confirming the presumption of deference toward annulment decisions in the primary jurisdiction. Moreover, it stresses that this presumption can only be rebutted in the most extraordinary of circumstances, which do not include disagreeing with the merits of the foreign judgment. Given this high hurdle, it will likely continue to be a rare case in which an annulled award will ever be enforced.

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[13] *Id*., at *10.
[14] *Id*., at *11.
[15] *Id*., at *10.
[16] *Id*., at *12.
[17] *Id*.