

## Public Policy Defense Rarely Bars Arbitral Award Enforcement

By **Ava Borrasso** (January 30, 2019, 9:08 PM EST)

In 2018, several U.S. courts were confronted with challenges to the enforcement of international arbitral awards pursuant to the oft-cited but rarely successful public policy defense set forth in Article V(2)(b) of the New York Convention.[1] Consistent with existing precedent, the defense failed most of the time it was advanced. This article highlights the unique circumstances in which the defense was advanced and the rare case in which it was successful (currently pending appeal).

Typically, as in most of the cases discussed here, the public policy defense is but one of several challenges to enforcement of an award. The focus on this article is limited to the analysis in these cases of the grounds upon which the public policy defense was raised and the resolution of the defense.

It is well-established that the public policy defense set forth in Article V(2)(b) of the New York Convention is narrowly construed by U.S. courts and requires that the party asserting it bear the heavy burden of demonstrating that enforcement of an award by a U.S. court would violate its “most basic notions of morality and justice.”[2] Given that heightened standard, perhaps it is not surprising that the defense rarely succeeds. That fact, however, has not impeded the ingenuity of those parties raising it.

### Public Policy Defense Based on Allegations of Underlying Fraud

A particularly interesting application, and one coming to the greater fore, is premised on allegations of underlying fraud in the proceedings. For example, in *Anatolie Stati v. Republic of Kazakhstan*,[3] Kazakhstan opposed enforcement of an arbitral award in excess of \$497 million entered in Sweden based, in part, on allegations of fraud in the underlying arbitration. Specifically, Kazakhstan contended that petitioners procured the award by fraud through the submission of false evidence and testimony to the arbitral tribunal that “materially misrepresented the [Plant] construction costs” for which they sought reimbursement.[4] In addition to other defenses raised by the issue, Kazakhstan argued enforcement of a fraudulently obtained arbitral award would be contrary to U.S. public policy.”[5]

The court applied the three-part test applicable to vacate a judgment for fraud under Section 10(a) of the Federal Arbitration Act to determine whether the alleged fraud constituted a sufficient basis to deny enforcement of the award as in violation of public policy. The requisite standard required the following: “(1) the movant must establish fraud by clear and convincing evidence; (2) the fraud must not have been



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discoverable upon the exercise of due diligence either before or during the arbitration; and (3) the person challenging the award must show that the fraud materially related to an issue in the arbitration.”[6]

The court rather easily determined that the purported fraud was not material to the outcome of the arbitration. Notably, Kazakhstan had sought to vacate the award in Sweden on fraud grounds. Kazakhstan maintained that the petitioners submitted false evidence in the arbitration proceeding regarding the value of the plant during the arbitration and, prior to the arbitration, misrepresented its investment in the plant in financial statements which caused a third party to bid in excess of the plant’s true value — a bid that the tribunal considered to value the plant. The Swedish courts denied vacatur reasoning that the alleged fraud was too remote and did not constitute fraud on the tribunal sufficient to annul the award.[7]

The U.S. district court stayed the enforcement case pending resolution of the Swedish challenge and its subsequent appeal. When the award was upheld in Sweden, the courts with primary jurisdiction over the matter, the U.S. court similarly determined that the alleged fraud was not sufficiently related to the decision. The district court also noted Kazakhstan’s delay of nearly a year after it purportedly had notice of the fraud before raising the issue to the court.

Similarly, in *De Rendon v. Ventura*, a U.S. district court denied the respondents’ public policy defense premised on fraud.[8] In that case, the respondents argued that they had entered a settlement agreement based on fraudulent representations by the petitioners valuing a pharmaceutical company at \$30 million that was sold two years later for over \$560 million. The terms of the confidential settlement agreement were subsequently breached by the respondents, resulting in arbitration proceedings, and ultimately an award against them.

When the respondents argued that the award should not be enforced due to the purported underlying fraud that procured the settlement agreement, the court determined the valuation was not relevant to breach of the settlement agreement’s confidentiality provisions. The court reasoned that although such evidence may pertain to the ongoing annulment proceedings of the main claim pending in Colombia, holding respondents “to the terms of their own purchase agreements” did not violate “basic notions of morality of justice.”[9]

### **Public Policy Defense Denied**

Other recent cases in which the public policy defense has been advanced and denied demonstrate the variety of instances in which it has been asserted. For example, the Republic of Ghana argued that enforcement of an arbitral award of \$11.75 million was contrary to the U.S. public policy to extend international comity to foreign court decisions.[10] The argument was premised on the Ghana Supreme Court’s decision that the underlying agreement violated Ghana’s constitution because it did not receive proper parliamentary approval and, therefore, the arbitration was improper.

In another instance, a Florida district court rejected application of the defense to an injured seaman’s claim that application of Panamanian law effectively deprived her of legal remedies under the Jones Act to pursue claims of vicarious liability based on the negligence of the treating physician selected by the cruise ship.[11] Although vicarious liability was unavailable pursuant to Panamanian law, the court determined that Panamanian law did provide adequate remedies which did not render enforcement of the choice of law provision fundamentally unfair. The court rejected the seafarer’s explanation that her failure to pursue those remedies was futile.[12]

## Public Policy Defense Upheld

In a rare case, the U.S. district court in Washington, D.C., denied enforcement of an arbitral award against the government of India as running afoul the Foreign Sovereign Immunities Act, or FSIA, and therefore, violating the strong U.S. policy favoring respect for the sovereignty of foreign governments. In *Hardy Exploration & Production (India) Inc. v. Government of India*,<sup>[13]</sup> the U.S. district court denied a petition to confirm an international arbitration award granting specific performance against India and declined to enforce a corresponding interest award.

The underlying agreement between the parties involved exploration rights for certain hydrocarbons within the territorial boundaries of India. The parties agreed that the time period to ascertain commercial viability depended on whether the hydrocarbons consisted of crude oil (two years) or natural gas (five years). When a dispute arose between the parties as to the type of the discovered hydrocarbons and India blocked the petitioner's continued access to the site, Hardy pursued arbitration. Hardy obtained an award for specific performance order requiring India to permit it access to the site and awarding pre-award interest to Hardy on its investment as well as additional interest at a higher rate until India's compliance with the terms of the award. The award was ultimately appealed to the Indian courts which appeared to be pending when Hardy filed its petition to confirm the award in the U.S.

The court ruled that a stay of the case was not proper and framed the issue as a conflict between two significant U.S. policies: enforcement of international arbitration awards and respect for foreign sovereignty. The court determined that extraterritorial confirmation of a specific performance award against a foreign sovereign for conduct within its boundaries was a clear violation of U.S. public policy as set forth in the FSIA and elsewhere.<sup>[14]</sup> Further, due to the coercive nature of the interest award and the fact that it was inextricably intertwined with the underlying specific performance award, the court also declined to enforce it. The court determined the unique aspects of the case presented "one of the limited circumstances" under which it could decline confirmation of a foreign arbitral award.

## Summary

Consistent with precedent, the 2018 cases in which enforcement of an international arbitration award was challenged by the public policy defense arose in a variety of circumstances and were rarely successful. The strong U.S. policy favoring the enforcement of foreign arbitration awards outweighs most circumstances in which it is challenged. While a heavy burden to meet, significant and countervailing policies must be weighed. As these 2018 U.S. court decisions foreshadow, the public policy defense will likely continue to be advanced in a variety of ever-changing circumstances and will succeed only in the rare case where fundamental U.S. principles of morality and justice are at issue.

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[1] Formally, the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

[2] E.g. *De Rendon v. Ventura*, No. 1:17-24380, 2018 WL 4501059 at \*5 (S.D. Fla. August 8, 2018).

[3] *Anatolie Stati v. Republic of Kazakhstan*, 302 F. Supp. 3d 187 (D.D.C. 2018), appeal filed, No 18-7047 (D.C. Cir. April 10, 2018).

[4] *Id.* at 193-94.

[5] *Id.*

[6] *Id.* at 199-200.

[7] *Id.* at 195-96.

[8] No. 17-24380, 2018 WL 4496300 (S.D. Fla. September 19, 2018), appeal filed, No. 18-14387 (11th Cir. October 17, 2018), adopting report and recommendation, No. 1:17-24380, 2018 WL 4501059 (S.D. Fla. August 8, 2018),

[9] 2018 WL 4501059 at \*6.

[10] *Balkan Energy Limited v. Republic of Ghana*, 302 F. Supp. 3d 144, 158-59 (D.D.C. 2018), appeal dismissed, 2018 WL 5115572 (D.C. Cir. October 12, 2018).

[11] *Corvo v. Carnival Corp.*, No. 16-21559, 2018 WL 1660669 at \*\*5, 6 (S.D. Fla. April 5, 2018), appeal filed, No. 18-11815 (11th Cir. April 30, 2018).

[12] In a prior decision, the same court adopted the magistrate judge's decision to deny a motion to dismiss finding that the plaintiff "should be allowed to pursue her Article V(2)(b) defense that the arbitral award violates the public policy of the United States because she was unable to vindicate her Jones Act claim in the arbitration." *Corvo v. Carnival Corp.*, 234 F. Supp. 3d 1220, 1233 (S.D. Fla. 2017). Ultimately, the court rejected the defense as detailed above.

[13] 314 F. Supp. 3d 95 (D.D.C. 2018), appeal filed, No. 18-7093 (D.C. Cir. July 6, 2018).

[14] The court held "forced interference with India's complete control over its territory violates public policy to the extent necessary to overcome the United States' policy preference for the speedy confirmation of arbitral awards." *Id.* at 113.