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Fifth Circuit Holds that Personal Jurisdiction is Required in New York Convention Recognition Proceedings

On December 21, 2012, the U.S. Court of Appeals for the Fifth Circuit issued its decision in *First Investment Corporation of the Marshall Islands v. Fujian Mawei Shipbuilding, Ltd.*,[i] in which that court addressed, for the first time, whether a proper basis of personal jurisdiction is necessary in order to grant a petition to confirm a foreign arbitration award under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention") and Chapter 2 of the Federal Arbitration Act. It held in the affirmative, reasoning that the requirement of personal jurisdiction is rooted in the United States Constitution and must be satisfied regardless of whether the New York Convention or its implementing legislation explicitly included such a requirement.

<u>Summary</u>

First Investment Corporation of the Marshall Islands ("First Investment") obtained an arbitration award against Fujian Shipbuilding Industry Group Corp. (FSIGC) and Fujian Mawei Shipbuilding Ltd. ("Mawei") (together, the "Fujian Entities"). FSIGC is 100%-owned by the People's Republic of China (PRC), and Mawei is a private corporation of which FSIGC is a majority shareholder. The arbitration took place in London and was conducted by a tribunal of three arbitrators. First Investment sought to confirm the award pursuant to the New York Convention in the Chinese courts, but encountered several difficulties along the way. As an example, First Investment claimed that the Chinese embassies in London and Athens initially refused to authenticate documents that were necessary for First Investment to commence a confirmation proceeding in China; however, upon the intervention of the Greek government, the Chinese embassy in Athens eventually acquiesced to provide the necessary authentication. First Investment also claimed that it was deprived, without explanation, the assistance of its Chinese counsel and its translator during a hearing before the Chinese court; instead the court provided First Investment with a student translator with a limited legal vocabulary. The Chinese court ultimately denied enforcement of the award on grounds that the arbitral tribunal was not constituted in accordance with the parties' agreement.

First Investment then commenced a confirmation proceeding in the Eastern District of Louisiana against the Fujian Entities and the PRC as well, on the ground that the Fujian Entities were each alter-egos of the PRC. The first default judgment entered by the district court against the Fujian Entities and

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the PRC was vacated for improper service. When a second default judgment was subsequently entered against the Fujian Entities and the PRC, the Fujian Entities filed a motion for reconsideration, and later a motion to dismiss, or in the alternative, to refuse to confirm the arbitral award. The district court granted the motion for reconsideration and vacated the default judgment against the Fujian Entities on June 28, 2011.[ii] On March 12, 2012, the district court also granted the motion to dismiss for lack of personal jurisdiction as to the Fujian Entities, and for lack of subject matter jurisdiction as against the PRC.[iii] First Investment appealed.

First Investment asserted that the district court erred with regard to its dismissal for lack of personal jurisdiction for the following reasons: first, that the Fujian Entities, foreign entities with no contacts in the United States, were not entitled to due process protections under the U.S. Constitution; and second, that lack of personal jurisdiction is not one of the seven exclusive grounds for non-recognition under the New York Convention, and that constitutional due process concerns therefore are not implicated in a confirmation proceeding under the New York Convention. The Court of Appeals disagreed with each of these propositions.

First, the Court rejected First Investment's argument that foreign entities that have neither a presence nor property in the United States are not entitled to due process protections, finding it to be foreclosed by the Supreme Court's decision in *Goodyear Dunlop Tires Operations, S.A. v. Brown*, 131 S.Ct. 2846 (2011), in which the Supreme Court implicitly held that foreign corporations without minimum contacts with the United States could still avail themselves of the protections of the Due Process Clause.

Second, the Court of Appeals rejected First Investment's arguments that due process concerns were not implicated by a New York Convention confirmation proceeding. While acknowledging that "lack of personal jurisdiction" was not one of the seven enumerated grounds for non-recognition of an arbitral award under the New York Convention, the Court of Appeals noted that "personal jurisdiction 'is 'an essential element of the jurisdiction of a district…court,' without which the court is 'powerless to proceed to an adjudication.''"[iv] The Court further explained that

> Even though the New York Convention does not list personal jurisdiction as a ground for denying enforcement, the Due Process Clause requires that a court dismiss an action, on motion, over which it has no personal jurisdiction…. Because the New York Convention, through its implementing legislation, is an exercise of presidential and congressional power, whereas personal jurisdiction is grounded in constitutional due process concerns, there can be no question that the Constitution takes precedence.[v]

The Court also noted that every other circuit to have considered the issue had found that a constitutionally-sufficient basis for personal jurisdiction was a mandatory prerequisite to the recognition of an arbitration award under the New York Convention.[vi] In joining these circuits, the Fifth Circuit adopted the Ninth Circuit's analysis in *Glencore Grain*, in which that court held that the absence of an explicit personal jurisdiction requirement in the New York Convention and its implementing legislation was irrelevant, because the personal jurisdiction requirement is based exclusively on the Due Process Clause.[vii]

The Court further disagreed that a confirmation proceeding under the New York Convention did not substantially affect the parties' substantive rights, noting that "First Investment misunderstands the significance of confirming an award." The Court explained that, with the advent of the New York Convention, the process for enforcing a foreign arbitral award was greatly simplified by permitting a party seeking to enforce an arbitration award to apply for confirmation in any foreign jurisdiction without first obtaining leave from the primary jurisdiction. The Court warned of several ways in which the parties' rights could be greatly affected under this simplified procedure; for example, the party seeking enforcement could "wholly [avoid] the New York Convention by converting the confirmation of an award into a court judgment that may be enforced abroad as a foreign judgment." The Court further recognized that "confirmation may result in a party losing the opportunity to raise defenses to enforcement that it might have raised at the confirmation stage" and "also makes it possible that a party, armed with a court judgment, will seek to enforce the award as a foreign judgment elsewhere….[which] may, for example, permit a party to circumvent the New York Convention's three-year statute of limitations."[viii] Thus, the Court concluded that due process protections were no less warranted in a New York Convention proceeding than in any other proceeding before a U.S. court.

First Investment also argued that the district court improperly dismissed its petition for lack of personal jurisdiction by failing to recognize that the Fujian Entities were alter egos of the PRC, which, as a foreign state, is not entitled to due process protections.[ix] The Court of Appeals opened its analysis by citing *First National City Bank v. Banco Para El Comercio Exterior de Cuba*, 462 U.S. 611, 103 S.Ct. 2591, 77 L.Ed.2d 46 (1983) ("*Bancec*"), as the "seminal case on the circumstance under which American courts may disregard the separate status of instrumentalities created by foreign governments."[x] Under *Bancec*, a court should look to several non-exhaustive factors in determining whether the presumption in favor of an entity's juridical independence should be disregarded, including "ownership and management structure of the instrumentality," "whether the government is involved in day-to-day operations," "the extent to which the agent holds itself out to be acting on behalf of the government," as well as whether respecting the corporate form "would lead to injustice."[xi] The Court of Appeals agreed with the district court that First Investment had not demonstrated that the presumption of separateness between FSIGC and Mawei, on the one hand, and the PRC, on the other, should be disregarded under that standard.

With regard to whether FSIGC could be considered an alter ego of the PRC, the primary evidence considered by the district court came through two declarations from different Chinese lawyers. While both declarations established that FSIGC was wholly-owned by the PRC, that a branch of the PRC appoints FSIGC's board of directors, and that the PRC exercises its rights as a shareholder, the declarations also conceded that FSIGC maintained independent operational and managerial authority, acted in the best interests of the company, filed independent financial statements, was responsible for its own debts, and dealt with the PRC in arms-length transactions. The Court Appeals found that such evidence fell short of the standard under *Bancec*, noting that "the mere fact that a government owns 100% of a company's stock is not sufficient to establish control."[xii] While First Investment submitted an additional declaration establishing that the PRC had affirmatively acted to try to prevent First Investment from enforcing its award against the Fujian Entities, the Court did not find such evidence persuasive, explaining that "whatever [the evidence of the PRC's obstructionism] says about the PRC's hostility toward foreign entities, it does not demonstrate the level of control necessary to overcome the presumption in favor of FSIGC's separate identity."[xiii] In response to First Investment's assertion that the district court failed to accord proper weight to equitable considerations, the Court of Appeals held that "it is not sufficient for [First Investment] to merely point out an injustice that would result from an adverse decision. Rather First Investment must show how the PRC manipulated FSIGC's corporate form to perpetuate a fraud or injustice."[xiv]

The Court found that the case for disregarding the corporate form of Mawei was even more attenuated, as it was owned by FSIGC, and any claim that Mawei was an alter-ego of the PRC would thus depend on whether FSIGC was an alter-ego of the PRC, a question that the Court had already answered in the negative. It also found that "First Investment has also not shown that the PRC manipulated Mawei's corporate form to commit a fraud or injustice."[xv]

Finally, the Court of Appeals addressed the propriety of the district court's determination that it lacked subject matter jurisdiction under the Foreign Sovereign Immunities Act (FSIA)[xvi] over the PRC. The Court of Appeals first explained that foreign states are generally immune from the jurisdiction of U.S. courts unless one of several statutorily defined exceptions applies. The Court noted that the parties did not dispute that only one such exception, 28 U.S.C. § 1605(a)(6),[xvii] which provides jurisdiction where an action is brought to enforce an agreement to arbitrate between a foreign state and a private party or to enforce any resulting award, could potentially apply in this case. Although the PRC was not a party to the arbitration, the district court considered whether it could be bound to the arbitration as an alter ego of the Fujian Entities. The Court of Appeals found that the district court properly determined that First Investment had failed to satisfy the *Bancec* standard for disregarding the presumption of separateness between the Fujian Entities and the PRC, and that, accordingly, First Investment's petition against the PRC was properly dismissed for lack of subject matter jurisdiction.

Comments and Conclusions

While the Fifth Circuit's decision comports with those of the Second, Third, Fourth, Seventh, Ninth, and Eleventh on the issue of whether personal jurisdiction is required in a confirmation proceeding under the New York Convention, the Court of Appeals' analysis was unique in some respects, particularly in its emphasis on the risks and potential abuses associated with the New York Convention's expedited enforcement procedures.

While the Court appeared to be guided by a view that the imposition of a personal jurisdiction requirement is a mandatory prerequisite for any adjudication by a U.S. court, the actual due process benefits of such a requirement in New York Convention cases are not entirely clear. Significantly, at least with respect to FSIGC,[xviii] a statutory ground for personal jurisdiction existed under Section 1330(b) the FSIA. Thus, the only matter left to be determined was whether such jurisdiction could be exercised in accordance with due process. *See Mwani v. bin Laden*, 417 F.3d 1, 8 (D.C. Cir. 2005) (in order for a court to exercise personal jurisdiction over a defendant, there must be both a statutory basis for the defendant's amenability to service of process and a constitutionally sufficient relationship between the defendant and the forum). Arguably, however, the true measure of due process in the context of a confirmation proceeding is whether fairness was afforded in the **underlying arbitration** – the proceeding in which the parties' substantive rights were adjudicated – and the New York Convention itself was designed to ensure that the parties to the arbitration received due process and that the underlying arbitration was fair, and further to ensure that the award will be promptly enforced by the courts of signatory states where the award meets the Convention's enforcement criteria.

The constitutional and statutory requirements underlying a U.S. court's exercise of personal jurisdiction are designed to protect a party from being haled into a distant court with which it lacks contacts and from the imposition of liability by a sovereign with whose laws it has no connection. However, where a party agrees to arbitrate a case in a New York Convention jurisdiction, it necessarily also agrees to the confirmation of any resulting award under the New York Convention. Further, unlike a party forced to defend a lawsuit in a foreign court, the party seeking to avoid confirmation of an arbitral award has already had its case adjudicated in accordance with an agreement it (presumably) entered into voluntarily. The confirmation proceeding merely seeks to enforce the resulting award through an expedited process that (1) the parties agreed to by agreeing to arbitrate in a New York Convention jurisdiction, and (2) which itself provides a party seeking to avoid confirmation an opportunity to present claims of unfairness in the arbitral process. In such circumstances, it is difficult to see the need for an additional due process check at the confirmation stage.

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[i] --- F.3d ---, No. 12-30377 (5th Cir. Dec. 21, 2012).

[ii] *See First Inv. Corp. v. Fujian Mawei Shipbuilding, Ltd*., No. 09–3663 (E.D. La. June 28, 2011).

[iii] *See First Inv. Corp. of the Marshall Islands v. Fujian Mawei Shipbuilding, Ltd. of People's Republic of China*, 858 F. Supp. 2d 658 (E.D. La. 2012).

[iv] *First Investment*, --- F.3d ----, at *5 (citing *Ruhrgas AG v. Marathon Oil Co*., 526 U.S. 574, 584 (1999).

[v] Id. at *5 (citations omitted).

[vi] Id. at *6 (citing *Frontera Res. Azer. Corp. v. State Oil Co. of Azer. Rep*., 582 F.3d 393, 397–98 (2d Cir. 2009) (confirmation proceeding under New York Convention requires personal or quasi in rem jurisdiction over parties); *Telcordia Tech Inc. v. Telkom SA Ltd*., 458 F.3d 172, 178–79 (3d Cir. 2006) (observing that "the New York Convention does not diminish the Due Process constraints in asserting jurisdiction over a nonresident alien"); *Base Metal Trading, Ltd. v. OJSC "Novokuznetsky Aluminum Factory"*, 283 F.3d 208, 212 (4th Cir. 2002) ("[W]hile the [New York] Convention confers subject matter jurisdiction over actions brought pursuant to the Convention, it does not confer personal jurisdiction when it would not otherwise exist."); *Glencore Grain Rotterdam B.V. v. Shivnath Rai Harnarain Co*., 284 F.3d 1114, 1121 (9th Cir. 2002); *see also S & Davis Int'l, Inc. v. Republic of Yemen*, 218 F.3d 1292, 1303–05 (11th Cir. 2000); *Emp'rs Ins. of Wausau v. Banco De Seguros Del Estado*, 199 F.3d 937, 941–43 & n. 1 (7th Cir. 1999) (requiring personal jurisdiction in dispute arising under Inter–American Convention on International Commercial Arbitration, but observing that result would be the same under New York Convention)).

[vii] *Id*. at *6 (citing *Glencore Grain*, 284 F.3d at 1121).

[viii] *Id*. at *7 (citations omitted).

[ix] While the Court of Appeals for the Fifth Circuit declined to explicitly so hold, it recognized that both the D.C. and Second Circuits had held that foreign states are not entitled to due process protections under the Fifth Amendment. *See id*. at *8 (citing *Price v. Socialist People's Libyan Arab Jamahiriya*, 294 F.3d 82, 96–97 (D.C. Cir. 2002) (reasoning that foreign states, like States of the Union, are not "persons" under the Fifth Amendment); *Frontera Res. Azer. Corp*., 582 F.3d at 399 (adopting reasoning in *Price*)).

[x] *Id*. at *8.

[xi] *Id*. at (citing *Walter Fuller Aircraft Sales, Inc. v. Republic of Philippines*, 965 F.2d 1375, 1381-2 (5th Cir. 1992)).

[xii] *Id*. at *9.

[xiii] *Id*. at *10.

[xiv] *Id*.

[xv] *Id*. at 11.

[xvi] Pub. L. 94-583, 90 Stat. 2891, 28 U.S.C. §§ 1330, 1332(a), 1391(f), 1601-1611.

[xvii] Section 1605(a)(6) provides specifically an exception to immunity in cases "to enforce an agreement made by the foreign state with or for the benefit of a private party to submit to arbitration all or any differences which have arisen or which may arise between the parties with respect to a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration under the laws of the United States, or to confirm an award made pursuant to such an agreement to arbitrate..."

[xviii] Although FSIGC was wholly-owned by the PRC, Mawei was majority-owned by FSIGC, which was insufficient to confer sovereign immunity on Mawei given that "only direct ownership of a majority of shares by the foreign state satisfies the statutory requirement." *Dole Food Co. v. Patrickson*, 538 U.S. 468, 474, 123 S.Ct. 1655, 1660 155 L.Ed.2d 643 (2003).