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New York Convention Awards In the **Second Circuit**

'Frontera' provides guidance on jurisdiction and foreign states.

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THE RECENT DECISION of the U.S. Court of Appeals for the Second Circuit in *Frontera Resources Azerbaijan Corp. v. State Oil Co. of Azerbaijan Republic*, 582 F.3d 393 (2d Cir. 2009), provides important guidance on the requirements of jurisdiction in proceedings to enforce international arbitral awards, and in actions against foreign states or their agents.

In *Frontera*, the Second Circuit determined that, before considering the exclusive grounds for refusing confirmation of an international arbitral award under Article V of the New York Convention,[1] federal courts in this circuit must determine that they have jurisdiction over the party (or the party's property) against whom enforcement is sought. The court further held that neither foreign states nor their agents are entitled to the jurisdictional protections of the Due Process Clause of the Fifth Amendment to the U.S. Constitution.

Both of these holdings break new ground in the jurisprudence of the Second Circuit, which had previously avoided deciding whether personal or quasi in rem jurisdiction was required in order to enforce a foreign arbitral award under the New York Convention. That question has now been definitively resolved and presents an important requirement that an award-creditor must consider before filing a petition to confirm an international arbitral award in this circuit.

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With respect to the constitutional protections available to foreign states, the circuit had previously held, for nearly 30 years, that a foreign state was a "person" for purposes of the Due Process Clause and was thus protected by the constitutional limitations on the power of the federal courts to exercise their jurisdiction. See *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*, 647 F.2d 300, 313 (2d Cir. 1981). After *Frontera*, that is no longer the law of this circuit. *Frontera* is part of a larger trend among U.S. courts to reject the status of a foreign state as a "person" for the purposes of the Due Process Clause.

This shift has potentially profound implications for foreign states, their agents, and the companies and individuals who litigate or arbitrate against them. It means that foreign states or their agents who have little or no connection to the United States may nevertheless be subject to suit in U.S. courts, including in proceedings to enforce international arbitral awards.

The 'Frontera' Dispute

In November 1998, Frontera Resources Azerbaijan Corp. (Frontera), a company based in the Cayman Islands, entered into an agreement with the State Oil Corporation of the Azerbaijan Republic (SOCAR) to develop and manage oil fields in Azerbaijan. Under the agreement, Frontera was to deliver to SOCAR the oil extracted from the fields that Frontera managed.

In 2000, a dispute arose over SOCAR's refusal to pay Frontera for some of the oil. When Frontera attempted to sell oil that was supposed to be sold to SOCAR to third parties outside of Azerbaijan, SOCAR seized it, leading Frontera to initiate an arbitration against SOCAR pursuant to the terms of their agreement.

An arbitral tribunal sited in Sweden issued an award in Frontera's favor. In February 2006, Frontera filed a petition in the Southern District of New York to confirm the arbitral award pursuant to Article II(2) of the New York Convention.

In assessing its jurisdiction for purposes of adjudicating the petition, the district court relied on the Foreign Sovereign Immunities Act (FSIA) as the statutory basis for jurisdiction over SOCAR.[2] The district court, while questioning whether SOCAR was entitled to the jurisdictional

protections of the Due Process Clause, followed the Second Circuit's decision in *Texas Trading* and dismissed Frontera's petition on the ground that SOCAR's contacts with the United States were insufficient to satisfy the requirements of due process. See *Frontera Res. Azer. Corp. v. State Oil Co. of Azer. Republic*, 479 F. Supp. 2d 376 (S.D.N.Y. 2007).

The district court also determined that it lacked quasi in rem jurisdiction because Frontera had not identified specific assets belonging to SOCAR within the district court's jurisdiction. Id. at 388.

On appeal, the Second Circuit held that the district court had correctly determined that jurisdiction over SOCAR or its property was a prerequisite to enforcement of the arbitral award in Frontera's favor, *Frontera*, 582 F.3d at 398, but it vacated the district court's dismissal of Frontera's petition on the ground that foreign states and their instrumentalities are not entitled to the jurisdictional protections of the Due Process Clause. Id. at 399.

The Jurisdiction Courts Must Have

As an initial matter, the Second Circuit rejected Frontera's contention that the district court need not establish personal or quasi in rem jurisdiction over the award-debtor or its property when considering a petition to enforce an arbitral award under the New York Convention.

Frontera had reasoned that Article V of the Convention provides the exclusive grounds for refusing confirmation of an international arbitration award, that lack of personal jurisdiction is not one of those grounds, and that the court may not impose a jurisdictional requirement that does not appear in the text of the convention. See id. at 397.

The Second Circuit dismissed this argument, noting that the defenses listed in the convention's Article V "pertain to *substantive* matters rather than to procedure," id. (emphasis in original), and that "jurisdictional questions ordinarily must precede merits determinations in dispositional order," id. (citation omitted).

Thus, the circuit concluded, while "Article V's exclusivity limits the ways in which one can challenge a request for confirmation," it "does nothing to alter the fundamental requirement of jurisdiction over the party against whom enforcement is being sought." Id. In so holding, the Second Circuit joined a number of its sister circuits that have similarly held that either personal or quasi in rem jurisdiction over the award-debtor or its property is a prerequisite to the enforcement of foreign arbitral awards under the New York Convention.[3]

But Is Due Process Applicable?

In its review of the district court's jurisdictional analysis, the Second Circuit noted that the parties did not challenge the district court's reliance on the FSIA as the statutory basis for jurisdiction over SOCAR; it focused instead on whether the district court had correctly concluded that SOCAR was a "person" for purposes of the Due Process Clause, and was thus entitled to benefit from constitutional limitations on the jurisdictional reach of the federal courts.

The Due Process Clause states that no "person" shall "be deprived of life, liberty or property, without due process of law." U.S. Const. amend. V. In the jurisdictional context, the clause requires that if a defendant "be not present within the territory of the forum, he have certain minimum contacts with it such that the maintenance of the suit does not offend traditional notions of fair play and substantial justice." *International Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945) (quotation marks and citation omitted).

> Before 'Frontera,' the Second Circuit had **avoided** deciding whether personal or quasi in rem jurisdiction was **required** in order to **enforce** a foreign arbitral award under the New York Convention.

For many years, courts reflexively applied the "minimum contacts" test to foreign states over which statutory jurisdiction existed under one of the FSIA's exceptions. The Second Circuit did so in *Texas Trading*, 647 F.2d at 313, and later applied the *Texas Trading* rationale to agents and instrumentalities of foreign states, *Seetransport Wiking Trader Schiffarhtsgesellshaft MBH & Co. v. Navimpex Centrala Navala*, 989 F.2d 572, 579-80 (2d Cir. 1993).

The Second Circuit in *Frontera* recognized that the district court's decision was compelled by *Texas Trading*, but, having noted that "the case law has marched in a different direction" since that case was decided,[4] it expressly overruled *Texas Trading*.[5] *Frontera*, 582 F.3d at 398, 400. In overruling *Texas Trading*, the Second Circuit largely adopted the reasoning of the D.C. Circuit in *Price v. Socialist People's Libyan Arab Jamahiriya*, 294 F.3d 82 (D.C. Cir. 2002).

Why Foreign States Are Not 'Persons'

Price concerned claims against Libya under two of the FSIA's exceptions to sovereign immunity relating to torture and hostage taking. See 28 U.S.C. §1605(a)(7). Under these exceptions, the only required nexus between the defendant foreign state and the territory of the United States is the nationality of the claimant, who must be a U.S. citizen.

Libya argued that foreign states, like private individuals and corporations, are entitled to the protections of the Due Process Clause, that it was undisputed that Libya had no connections with the United States, that the required "minimum contacts" were therefore lacking, and that the claims against it must be dismissed. *Price*, 294 F.3d at 95. The D.C. Circuit rejected Libya's premise that foreign states are "persons" protected by the Due Process Clause.

In making this determination the D.C. Circuit relied on the U.S. Supreme Court's decision in *South Carolina v. Katzenbach*, 383 U.S. 301 (1966), in which the Court found that U.S. states are not "persons" for due process purposes. *Price*, 294 F.3d at 96. The *Price* court reasoned that, if U.S. states are not "persons" entitled to due process protections, then "absent some compelling reason to treat foreign sovereigns more favorably than 'States of the Union,' it would make no sense to view foreign states as 'persons' under the Due Process Clause." Id.

The Second Circuit in *Frontera* relied heavily on this reasoning. It noted that "States of the Union both derive important benefits [from the Constitution] and must abide by significant limitations as a consequence of their participation [in the Union]," whereas foreign states lie outside this structure. *Frontera*, 582 F.3d at 399 (quoting *Price*, 294 F.3d at 96). The Second Circuit, like the D.C. Circuit, could not "see why foreign states, as sovereigns wholly outside the Union, should be in a more favored position" than U.S. states, particularly where courts have always relied on notions of comity and international law to protect foreign states in the American legal system, not on rights derived from the Constitution. Id.

But the Second Circuit's conclusion "that foreign states are not 'persons' entitled to rights under the Due Process Clause," id. at 400, did not decide the ultimate question before the court because the defendant in *Frontera*, SOCAR, was not a foreign state, but merely an instrumentality or agent of one. The circuit noted that, while the FSIA treats foreign states the same as their instrumentalities or agents, the U.S. Constitution may not. Id.

With respect to SOCAR, the Second Circuit

concluded that, "if the Azerbaijani government exerted 'sufficient control over' SOCAR 'to make it an agent of the State, then there is no reason to extend to SOCAR a constitutional right that is denied to the sovereign itself.'" Id. at 400 (quoting *TMR Energy Ltd. v. State Prop. Fund of Ukr.*, 411 F.3d 296, 301 (D.C. Cir. 2005)) (alterations incorporated).

The Second Circuit remanded the case back to the district court to determine whether "sufficient control" existed such that SOCAR was an agent of Azerbaijan. If so, then, "like Azerbaijan, SOCAR [would] lack[] due process rights," id. at 400, and would not be entitled to a "minimum contacts" analysis. If not, the district court was instructed to determine whether SOCAR, as a corporation owned by a foreign state but not an "agent" of a foreign state, was entitled to due process protections. The parties settled before the district court decided these issues on remand.

Implications for Practitioners

The Second Circuit's *Frontera* decision has important implications for practitioners of international litigation and arbitration in the circuit.

First, it is now clear that courts in the Second Circuit will require a showing of either personal or quasi in rem jurisdiction before they will enforce an international arbitral award under the New York Convention. This jurisdictional requirement must be satisfied even though lack of jurisdiction of the enforcing court is not a ground for refusing enforcement under Article V of the Convention.

While this decision resolves an important issue that the circuit had long avoided deciding, and makes clear that award-creditors must be careful to ensure that jurisdiction may be obtained before filing a petition to confirm an arbitral award, the practical implications of the decision are less obvious.

It is not clear that this ruling will have much impact on the decision of award-creditors to attempt to enforce arbitral awards in New York federal courts, or other courts within the Second Circuit, since it is likely that they would choose to do so in circumstances in which the award-debtor already had assets in the jurisdiction or at least substantial ties to it. To the extent that award-creditors may wish to confirm international arbitral awards in the courts of the Second Circuit in the absence of such assets or jurisdictional ties, for example, so that they may be in a position to enforce the award when the award-debtor's assets pass through the forum,[6] such efforts are now definitively foreclosed.

The circuit's reversal of *Texas Trading*, and its finding that foreign states and their agents are not subject to the jurisdictional protections of the Due Process Clause, may ultimately have more practical significance. *Frontera* represents a significant change for litigants who do business with foreign states that maintain few connections with or activities in the United States. Those entities may no longer avoid the jurisdiction of federal courts in the Second Circuit based on their lack of minimum contacts with the United States.

This will presumably make the courts of this circuit a more attractive jurisdiction in which to bring actions against foreign states and their agents, including proceedings to enforce international arbitral awards. That said, the defense of forum non conveniens remains fully applicable in FSIA cases, including proceedings to enforce arbitral awards under the New York Convention, and continues to impose significant limits on the availability of U.S. courts to foreign litigants.[7]

Finally, *Frontera* leaves a number of significant issues open for resolution another day. It remains undecided, for example, whether companies that are owned by a foreign state, but that are not so controlled by the state that they may be considered its "agents," are entitled to due process protections. The D.C. Circuit has called this question "far from obvious" based on its observation that "'aliens receive constitutional protections [only] when they have come within the territory of the United States and developed substantial connections with this country.'" *TMR Energy*, 411 F.3d at 302 n.* (quoting *United States v. Verdugo-Urquidez*, 494 U.S. 259, 271 (1990)).

Yet, as the Second Circuit noted in *Frontera*, the Supreme Court has long accorded due process protections to privately owned foreign corporations. See *Helicopteros Nacionales de Colombia, S.A. v. Hall*, 466 U.S. 408, 418-19 (1984). The answer to this question will have additional important implications for foreign states and state entities, and the parties who bring claims against them.

1. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2417, implemented at 9 U.S.C. §207.

2. Congress enacted the FSIA in 1976 to provide the "sole basis for obtaining jurisdiction over a foreign state," including the state's agents and instrumentalities, in U.S. courts. See *Argentine Republic v. Amerada Hess Shipping Corp.*, 488 U.S. 428, 434 (1989). The FSIA provides immunity from suit unless one of a number of exceptions apply. One prominent exception is made for the enforcement of arbitration awards governed by a treaty, such as the New York Convention. 28 U.S.C. §1605(a)(6)(B). Other exceptions to sovereign immunity are triggered where, inter alia, the foreign sovereign has waived its immunity, 28 U.S.C. §1605(a)(1), or the foreign sovereign has engaged in "commercial activity," 28 U.S.C. §1605(a)(2). See *Verlinden B.V. v. Cent. Bank of Nig.*, 461 U.S. 480, 488-89 (1983).

3. See, e.g., *Telcordia Tech Inc. v. Telkom SA Ltd.*, 458 F.3d 172, 178-79 (3d Cir. 2006); *Glencore Grain Rotterdam B.V. v. Shivnath Rai Harnarain Co.*, 284 F.3d 1114, 1120-22 (9th Cir. 2002); *Base Metal Trading, Ltd. v. OJSC "Novokuznetsky Aluminum Factory,"* 283 F.3d 208, 212-13 (4th Cir. 2002).

4. The Supreme Court had raised doubts about applying the protections of the Due Process Clause to foreign states in *Republic of Argentina v. Weltover Inc.*, 504 U.S. 607 (1992), in which it "assume[d], without deciding, that a foreign state is a 'person' for the purposes of the Due Process Clause," id. at 619, but noted that "States of the Union are not 'persons' for the purposes of the Due Process Clause." Id. A few years later, the Second Circuit noted that "since the Supreme Court decided *Weltover*, we are uncertain whether our holding [in *Texas Trading*] remains good law." *Hanil Bank v. PT. Bank Negara Indon. (Persero)*, 148 F.3d 127, 134 (2d Cir. 1998). Despite these doubts, the Second Circuit reaffirmed *Texas Trading* in its decision in *U.S. Titan Inc. v. Guangzhou Zhen Hua Shipping Co.*, 241 F.3d 135, 152 (2d Cir. 2001), in which it noted that "the exercise of personal jurisdiction under the FSIA must also comport with the Due Process Clause."

5. The panel that decided *Frontera* recognized that "our court's decisions are binding until overruled by us sitting en banc or by the Supreme Court," but undertook a "mini-en banc" process, in which the *Frontera* panel circulated the opinion among all active members of the Second Circuit, none of whom objected. *Frontera*, 582 F.3d at 399-400.

6. See G. Born, International Commercial Arbitration 2403 n.388 (3d ed., Kluwer Law International, 2009).

7. See *Frontera*, 582 F.3d at 402 (noting that SOCAR was free, on remand, to raise its forum non conveniens argument, which the district court had declined to address in the first instance in light of its jurisdictional determination); see also *Monegasque de Reassurances S.A.M. v. NAK Naftogaz of Ukr.*, 311 F.3d 488, 496 (2d Cir. 2002) (affirming dismissal of petition to confirm arbitral award under the FSIA and New York Convention on grounds of forum non conveniens); but see G. Born, International Commercial Arbitration 2402 (3d ed. 2009) ("Prima facie…the refusal of a Contracting State's courts to enforce an award on forum non conveniens grounds is contrary to the New York Convention").