Cayman Islands Court of Appeal enforces foreign arbitral award in favour of Brazilian airline

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The Court of Appeal of the Cayman Islands has overturned the earlier decision of the Grand Court, thereby allowing the enforcement of a R$92,987,672 ICC arbitration award, issued in 2007 in favour of a Brazilian airline. The Brazilian ICC arbitration award was decided under Brazilian law and upheld by the Brazilian courts in annulment proceedings brought by the award debtors. The Court of Appeal has now held that the award debtors and respondents to the appeal are estopped from challenging enforcement of the award by virtue of Brazilian court decisions, in which the various challenges had already been raised and dismissed.

Ogier successfully acted for the appellant in this appeal, Brazil's Gol Linhas Aereas SA (**Gol**), with Leading Counsel, Thomas Lowe QC of Wilberforce Chambers, and Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados of Brazil.

The decision raises important and difficult issues relating to the enforcement of foreign arbitral awards which are the subject of robust challenge before the courts of supervisory jurisdiction. In particular, the decision is likely to be of particular interest to practitioners in common law jurisdictions who seek to enforce arbitral awards obtained in civil law jurisdictions.

Background Facts

The respondents, Matlinpatterson Global Opportunities Partners (Cayman) II LP, Matlinpatterson Global Opportunities Partners II LP and their general partner, Matlinpatterson Global Partners II LLC (collectively, the **MP Funds**) are private investment funds that specialise in "distressed investing". In 2005, the MP Funds established Volo Logistics, a Delaware company to serve as an investment vehicle for pursuing an opportunity in the Brazilian aviation industry. Volo Logistics, and three Brazilian investors, established Volo do Brasil SA (**Volo dB**) which, in

2006, purchased Varilog Logistica SA (**Varilog**) which operated a Brazilian cargo airline. Later in 2006, Volo dB and Varilog then purchased a Brazilian passenger airline through a special purpose vehicle VRG Linhas Aereas SA (**VRG**).

Pursuant to a Share Purchase and Sale Agreement dated 28 March 2007 (**PSA**), Volo dB and Varilog (the **Sellers**) sold 100% of their shares in VRG to a Brazilian company, GTI SA (**GTI**, the **Purchaser**). GTI was subsequently merged into VRG, which has now been renamed GoI. The MP Funds were not parties to the PSA containing the arbitration agreement, which provided for an ICC arbitration with its seat in São Paulo, but subsequently signed an addendum which joined them to a non-compete provision in the PSA.

A dispute subsequently arose concerning the working capital of GTI (or VRG, as it had become) and a demand for an adjustment to the purchase price paid under the PSA. VRG commenced an arbitration against not only the sellers (Varilog and Volo dB) but also the MP Funds, premised on the MP Funds' fraudulent misuse of the sellers in the sale of the airline. VRG argued that the corporate veil should be lifted, as the MP Funds *"*were the alter egos of Varilog and Volo dB".

The MP Funds argued from the outset that they were not parties to the PSA and therefore disputed the arbitrators' jurisdiction over them (alternatively, they argued that even if they were, the scope of any arbitration agreement could not extend beyond their non-compete obligations in the PSA). In April 2009, the arbitral tribunal, exercising their rights of competence competence, issued a partial award rejecting the MP funds' jurisdictional objections (the **Partial Award**). The following year, in September 2010, the tribunal issued a final award finding that fraud had been proven (the **Final Award**). The tribunal held the sellers liable for R$92,987,672 under the price adjustment clause of the PSA, and although it rejected VRG's claim that the MP Funds were alter egos of the sellers, it found them liable on the basis of a tort in article 148 of the Brazilian Civil Code "third party malice" (**Article 148**). They did so pursuant to the civil law doctrine of "iura novit curia", a fundamental and well known doctrine of Brazilian practice, which means that a court (as opposed to the parties) is charged with applying the law to the facts.

The MP Funds commenced an action before the Brazilian courts for a review of the Partial Award as to the tribunal's jurisdiction, and challenged the Final Award on the grounds of lack of due process as a result of the tribunal's reliance on Article 148. The MP Funds were unsuccessful at first instance, and their appeal to the São Paulo Court of Appeals, and subsequent applications for leave to appeal to the Brazilian Supreme Court, were dismissed.

Cayman Islands law regarding the enforcement of foreign arbitral awards and the first instance decision

The rules on enforcement of foreign arbitral awards in the Cayman Islands are contained in the Foreign Arbitral Awards Enforcement Law (1997 Revision) (the **Enforcement Law**), which gives domestic effect to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Pursuant to this statutory regime, all foreign awards are enforceable in the Cayman Islands subject to the leave of the Grand Court. The grounds upon which the Cayman court may refuse the enforcement are limited to those set out in section 7(2) of the Enforcement Law, which mirrors Article V of the New York Convention. Section 7(3) of the Enforcement Law also provides that recognition and enforcement may be refused where it would be contrary to public policy.

GoI sought and initially obtained, on an ex-parte basis, leave to enforce the Final Award against the MP Funds in the Cayman Islands. However, this order was subsequently set aside by Justice Mangatal at the inter-partes stage.

Enforcement of the Final Award was strenuously challenged before Justice Mangatal on four grounds, namely: (i) the MP Funds were not parties to the arbitration agreement and had not consented to arbitration; (ii) if they were, the claims raised in arbitration were outside the scope of the arbitration agreement; (iii) the arbitral tribunal had decided the case on a legal ground (Article 148) that had never been pleaded or argued, which offends the principle of natural justice; and (iv) the legal ground relied upon was not within the terms of reference of the arbitration, so had not been submitted to arbitration. The Judge agreed with all four grounds, and therefore refused to enforce the award in the Cayman Islands. In doing so, she rejected GoI's arguments based on (1) Brazilian law (as reflected in the Brazilian courts' decisions and the evidence of Brazilian law experts deployed) and (2) the submission of estoppel, based on the Brazilian courts' decisions.

The Court of Appeal decision on estoppel

GoI's appeal focussed almost exclusively on its argument of estoppel. At first instance, the Judge rejected GoI's submission of estoppel for three reasons:

a. by reason of article 502 of the Brazilian Code of Civil Procedure (**Article 502**), [1] there can be no res judicata while the Brazilian annulment proceedings remain under appeal

b. the issues in the Brazilian courts and in the Cayman Islands were in any event not identical

c. the issue of public policy (the standards of natural justice) is in any event a matter for Cayman Islands law

The Cayman Islands Court of Appeal overturned each of these findings, which are discussed below. However, before doing so, the Court of Appeal took the opportunity to clarify the nature of the forensic examination that is required by the enforcing court in circumstances were there has already been a challenge to the arbitrators' jurisdiction in the supervisory courts.

The leading English authority is *Dallah Real Estate and Tourism Holding Co v Ministry of Religious Affairs of the Government of Pakistan* [2010] UKSC 46. In that case, the English courts applied French law to determine whether the arbitral tribunal had correctly found, in its initial award on jurisdiction, that the Government of Pakistan was a party to the arbitration agreement. The English Commercial Court, Court of Appeal and Supreme Court, applying French law, all held that the tribunal had erred, and the Government of Pakistan was not a party to the agreement, and refused enforcement. However, much to the English courts' embarrassment, the award was subsequently enforced in France: the English courts had got French law wrong.

The Court of Appeal emphasised that this was not surprising, particularly given that there are key differences between civil law and common law jurisdictions on the principles of contractual interpretation. [2] Further, the Court of Appeal surmised that *had* the French enforcement proceedings preceded the English proceedings, or if the Government of Pakistan had previously unsuccessfully challenged the jurisdiction of the arbitrators in the French courts, it is impossible to think that the English courts would have erred in their findings of French law. This was exactly the situation in the present case: the Brazilian courts had already reviewed, and dismissed the MP Funds' challenge to the Partial Award, and yet the Judge had differed from the Brazilian courts in her findings of Brazilian law.

The tribunal's rights of competence competence always remain subject to the challenge in the courts, and the court's review is to be conducted "de novo". As per Lord Mance in *Dallah*: "a party who has not submitted to the arbitrator's jurisdiction is entitled to a full judicial determination on evidence of an issue of jurisdiction before the English court". [3] However, the Court of Appeal stressed that the position fundamentally changes once the tribunal's jurisdiction has already been reviewed by the court of supervisory jurisdiction, or once the award has been subject to enforcement proceedings in that country. At that stage, the court is not dealing with the preliminary competence competence views of a tribunal, but with a judgment of a court, whose jurisdiction is not in question.

It is trite law that to establish a plea of estoppel, there must be (i) a judgment of (a) a court of competent jurisdiction, which was (b) final and conclusive and (c) on the merits; (ii) identity of parties, and (iii) the same issue in both actions. [4]

The Court of Appeal was first tasked with deciding whether the Brazilian court decisions were "final and conclusive", and addressing the clash between Article 502 - which provides that, as a matter of Brazilian law, any judgment under appeal is not "res judicata" - and the English authorities, which make clear that the prospect of appeal is irrelevant to any judgment being final and conclusive: *Nouvion v Freeman* [5] and *The Sennar (No 2).* [6]

The leading English decision is *Nouvion* which draws a distinction between a judgment which could be re-opened in other proceedings (which is not final and conclusive) and one which is merely susceptible to appeal (which is). Applying this distinction to this case, the question was

whether the MP Funds were correct that Article 502 was conclusive evidence, derived from Brazilian law, that any Brazilian judgment under appeal is not "final and conclusive", or whether Article 502 did not effect a Brazilian judgment being "final and conclusive" in the sense defined in *Nouvion*.

The Court of Appeal held that, ultimately, the doctrine of estoppel is a matter of the lex fori, ie in this case Cayman Islands law, and that the English test should predominate.

The second issue which the Court of Appeal addressed was whether the Judge had correctly rejected an estoppel on the basis that the issues before the English and Brazilian courts were not identical. The Court of Appeal found that the Judge below had erred in her approach: after concluding (incorrectly) that Brazilian courts are not required to reach a decision de novo on the question of jurisdiction, the Judge then applied her own views of contractual interpretation under Brazilian law, paying no regard to the Brazilian courts' views.

The Court of Appeal held that the issues decided by the Brazilian courts were the same issues that would arise on the MP Funds' defences under the New York Convention and Enforcement Law. In those circumstances, the Brazilian judgments were plainly the best evidence there is of Brazilian law and of what a Brazilian court would decide, and are therefore determinative. Once it was accepted that the Brazilian judgments were decisions as to the same matters that were before the Cayman courts, it was inappropriate to go behind them.

On this basis, the Court of Appeal held that MP Funds were estopped from challenging the Brazilian court decisions handed down on the arbitrators' jurisdiction.

Should the award not be enforced on due process and policy grounds?

The parties agreed that the question as to whether enforcement should be refused on public policy grounds is a matter of Cayman Islands law.

However, the leading English authorities establish that, where due process is concerned, although the standards are ultimately those for the home court to set, proper regard must be had for the foreign procedure and what the foreign courts have to say about the issue of due process: *Adams v Cape Industries* [7] and *Minmetals.* [8] This is particularly so when one is looking at the civil law system, and in this case, it was necessary to have a proper understanding of Brazilian procedure, and in particular the doctrine of iura novit curia.

Sir Bernard Rix JA of the Court of Appeal carefully considered the doctrine of iura novit curia in international law, and concluded that the doctrine is standard in the civil law (even though it is not practised in the common law world) and it is impossible to say that Brazilian law does not recognise the doctrine within international arbitration, seated in Brazil. A distinction may have

to be drawn between cases where the doctrine answers the due process question of the right to be heard, and cases where a reasonable and conscientious party has been unfairly caught by surprise, and derived of substantial or natural justice. The Court of Appeal concluded that the doctrine of iura novit curia was so widespread and well recognised in the civil law, that they would be concerned if English and Cayman Islands law would seek to ignore it when determining whether or not to allow the enforcement of an arbitral award from a civil law jurisdiction.

Further, the Court of Appeal noted that there has been no case in which an award has been challenged, but upheld, in the supervisory court on due process grounds, and then enforcement has been rejected on the same due process challenge. There has also been no similar case in which a major doctrine of the civil law, such as the doctrine of iura novit curia, has been rejected as contrary to substantial justice under English (or Cayman Islands) law.

The Court of Appeal acknowledged that the question of whether a New York Convention or Enforcement Law defence, whether of due process or public policy, had been made out in these circumstances was novel to English and Cayman jurisprudence, and the question was difficult and challenging. However, the Court of Appeal concluded that the defence had not been proven and was persuaded by the fact that the Brazilian courts (and the ICC Court of Arbitration) had considered the arbitrators' deployment of the doctrine without finding a breach of due process, which was significant. Further, where the Cayman or English court has to consider a due process challenge to the enforcement of a foreign award rendered under a foreign law, it is necessary to show that substantial injustice might have been caused, so that a significant difference of outcome may have resulted: the Court of Appeal was not persuaded that had occurred in this case.

Conclusion

In conclusion, the Court of Appeal allowed GoI's appeal, overturning the decision of the lower court in its entirety. However, given that it is possible (albeit, the Court of Appeal acknowledged unlikely) that the MP Funds could ultimately succeed in their remaining outstanding appeal to the Supreme Court in Brazil, the Court of Appeal granted a stay of execution pending the outcome of the Brazilian appeal, pursuant to section 7(5) of the Enforcement Law.

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[1] Article 502 of the BCCP provides "Substantive res judicata is the authority that renders

immutable and indisputable a decision on [the] merits that is no longer subject to appeal".

[2] These key differences have been authoritatively discussed in *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38, see Lord Hoffman at [39]

[3] See *Dallah* at [26]

[4] *Carl Zeiss Stiftung v Rayner & Keeler Ltd* [1967] 1 AC 853 (HL)

[5] *Nouvion v Freeman* (1889) App Cas 1

[6] *The Sennar (No 2)* [1985] 1 WKE

[7] *Adams v Cape Industries plc* [1990] Ch 433

[8] *Minmetals Germany GmbH v Ferco Steel Ltd* [1999] 1 All ER (Comm) 315

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