

Philippine Supreme Court Refuses Confirmation of Domestic Arbitral Award on Public Policy Grounds

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Introduction

Philippine courts are generally allowed to vacate or set aside an arbitral award issued in a domestic arbitration or an international commercial arbitration seated in the Philippines if it has been clearly shown that the award suffers from any of the infirmities or grounds for vacating an award under:

1. **For arbitral awards issued in domestic arbitrations:** Section 24 of Republic Act No. 876 or the *Domestic Arbitration Law* ("**Domestic Arbitration Law**"), Rule 34 of the UNCITRAL Model Law on International Commercial Arbitration ("**Model Law**"), or Rules 11.4 and 19.10 of A.M. No 07-11-08-SC or the *Special Rules of Court on Alternative Dispute Resolution* ("**ADR Rules**"); or
2. **For arbitral awards issued in international arbitrations seated in the Philippines:** Rule 34 of the Model Law or Rules 12.4 and 19.10 of the ADR Rules.

These grounds include if the recognition or enforcement of the arbitral award would be contrary to Philippine public policy. This rule is similar to Article V(2)(b) of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("**New York Convention**"), which allows a court to refuse the recognition or enforcement of a foreign arbitral award if doing so would be contrary to the public policy of the country where enforcement is sought.

In a Decision dated 7 December 2021 (but which was only published on 22 May 2023) in *Maynilad Water Services Inc. ("Maynilad") v. National Water and Resources Board ("NWRB") et al.* (G.R. Nos. 181764, 187380, 207444, 208207, 210147, 213227, 219362, and 239938, December 7, 2021) ("**Maynilad Case**"), the Philippine Supreme Court ("**SC**"),

sitting *en banc*, overturned the decisions of the lower courts and refused to confirm a domestic arbitral award rendered by a three-person arbitral tribunal in favor of Maynilad, as its confirmation or recognition would violate Philippine public policy. The SC in the *Maynilad Case* also confirmed that the ADR Rules superseded the provisions of the Domestic Arbitration Law on the reglementary period for filing petitions for confirmation of domestic arbitral awards.

Background

The dispute in the *Maynilad Case* arose when Metro Manila water concessionaires, Maynilad and Manila Water Company, Inc. ("**Manila Water**") petitioned unsuccessfully to increase their water rates in their respective concession agreements with the Philippine government. The Metropolitan Waterworks and Sewerage System Regulatory Office ("**MWSS**") held that Manila Water and Maynilad were prohibited from including their corporate income tax ("**CIT**") as expenditure recoverable from water consumers. In response, Manila Water and Maynilad instituted separate domestic arbitration proceedings against MWSS pursuant to Article 12 of their respective concession agreements.

Manila Water was unsuccessful in its arbitration, with the tribunal ruling that its CIT was not an allowable expenditure. Conversely, in the arbitration filed by Maynilad, the tribunal held that Maynilad may recover its CIT by way of tariff. Maynilad then filed a petition with the trial court for the confirmation of the domestic arbitral award.

MWSS opposed the confirmation of the award on the grounds of public policy. Among others, MWSS argued that confirmation would result in a disproportionate price difference between the water rates in the areas in Metro Manila serviced by Maynilad (*i.e.*, West Service Area), and those serviced by Manila Water (*i.e.*, East Service Area), which would be contrary to the equal protection clause of the Philippine Constitution. The trial court confirmed the award and its decision on the matter was affirmed by the Court of Appeals, thus prompting MWSS to elevate the matter to the SC. MWSS further argued that the trial court should not have confirmed the arbitral award in favour of Maynilad because it was filed beyond the 30-day period provided in section 23 of the Domestic Arbitration Law.

Establishing Violation of Public Policy Considerations

Before the promulgation of the decision in the *Maynilad Case*, the SC, in *Mabuhay Holdings Corporation v. Sembcorp Logistics Limited* (G.R. 212734, December 5, 2018) ("**Mabuhay Case**"), adopted the "narrow and restrictive approach" in determining whether the enforcement of a foreign arbitral award would be contrary to Philippine public policy. Citing Article V of the New York Convention, the SC in the *Mabuhay Case* held that a court may refuse to enforce a foreign arbitral award if doing so would violate Philippine public policy. According to the SC in the *Mabuhay Case*, a violation of Philippine public policy would be established where the consideration or thing to be done under the award:

1. has the tendency to injure the public;
2. is against the public good;
3. contravenes some established interests of society;
4. is inconsistent with sound policy and good morals; or
5. tends clearly to undermine the security of individual rights, whether of personal liability or of private property.

The SC in the *Mabuhay Case* held that "*Mere errors in the interpretation of the law or factual findings would not suffice to warrant refusal of enforcement under the public policy ground. The illegality or immorality of the award must reach a certain threshold such that, enforcement of the same would be against [the Philippines'] fundamental tenets of justice and morality, or it would blatantly be injurious to the public, or the interests of the society.*"

The *Mabuhay Case* involved a petition to enforce a foreign arbitral award. Nonetheless, the SC applied the foregoing standard in the *Maynilad Case*, which involved a petition for the confirmation of a domestic arbitral award, but with differing results.

In the *Mabuhay Case*, the SC held that the enforcement of the foreign arbitral award in favor of Sembcorp would not be contrary to Philippine public policy. On the other hand, the SC in the *Maynilad Case* ruled that the confirmation of the domestic arbitral award in favor of Maynilad would be contrary to Philippine public policy. The SC in the *Maynilad Case* noted that recognizing and enforcing the arbitral award in the *Mabuhay Case* would have had no injurious effect to the public, but that allowing Maynilad to include its CIT in the computation of water rates would adversely affect the public for the following reasons:

1. Maynilad and Manila Water, as public utilities, are expressly prohibited from passing their CIT on to consumers as operating expenses. A public utility, not the consumers, enjoys the privilege of earning income. Hence, the tax on that privilege should be shouldered by the public utility, not the consumers. The rates resulting from the arbitral award would thus be both unjust and inequitable, violating Republic Act No. 6234; and
2. The resulting increase in rates for consumers served by Maynilad would result in unequal protection compared to those served by Manila Water, even though there was no substantial distinction between the consumers in the two areas.

Limitation Period for Filing Petition for Confirmation

With regard to Maynilad's petition for confirmation, the SC considered this to have been filed in a timely manner.

Section 23 of the Domestic Arbitration Law states: "*At any time within one month after the award is made, any party to the controversy which was arbitrated may apply to the court having jurisdiction, as provided in section twenty-eight, for an order confirming the award.*"

The SC explained that while Republic Act No. 9285, or the *Alternative Dispute Resolution Act of 2004* ("**ADR Act**"), declares that domestic arbitration shall continue to be governed by the Domestic Arbitration Law, the ADR Act also states that its provisions are "*without prejudice to the adoption by the Supreme Court of any ADR system, such as mediation, conciliation, arbitration, or any combination thereof ... which shall be governed by such rules as the Supreme Court may approve from time to time.*"

In this regard, Rule 11.2(A) of the ADR Rules provides that "*At any time after the lapse of thirty (30) days from receipt by the petitioner of the arbitral award, he may petition the court to confirm that award.*" According to the SC in the *Maynilad Case*, section 23 of the Domestic Arbitration Law is deemed superseded by Rule 11.2(A) of the ADR Rules on the reglementary period for filing petitions for confirmation of domestic arbitral awards.

Concluding Remarks

Maynilad confirms that Philippine courts may set aside an arbitral award issued in a domestic arbitration or an international commercial arbitration seated in the Philippines if it has been clearly shown that confirmation or recognition of the award will violate Philippine public policy. It also provides a clear example of what constitutes a violation of public policy, *i.e.*, where confirming the award would prove injurious or detrimental to the public and would violate the Philippine Constitution. The decision also clarifies that petitions to confirm domestic arbitral awards should be filed after the lapse of 30 days from receipt of the award.

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