

# Kluwer Arbitration Blog

## Arbitrability and Enforcement in the Philippines: The Maynilad Case

Angela Ray T. Abdala (Singapore International Dispute Resolution Academy) · Monday, October 23rd, 2023

The Philippine Supreme Court recently issued a decision in *Maynilad Water Services, Inc., v. National Water and Resources Board, et al.*, where the Court ruled that (1) disputes concerning changes in water rates charged to consumers are arbitrable and that (2) arbitral awards that would be injurious to the public at large cannot be enforced under the public policy exception.

This case involved domestic arbitration, but the Court's decision has implications for international arbitration as well. While the ruling is a welcome development, it seems to offer a potentially problematic inconsistency as to whether certain awards that cover arbitrable disputes can survive the public policy analysis and be enforced in the Philippines.

### Background

The Metropolitan Waterworks and Sewerage System ("MWSS") is a government owned and controlled corporation that oversees waterworks and sewerage systems in Metro Manila. The law mandates MWSS to periodically fix water rates and sewage service fees in a just and equitable manner.

The MWSS entered into two separate Concession Agreements with private companies to maintain the water and sewerage systems in Metro Manila. Maynilad was put in charge of Service Area West and Manila Water maintained Service Area East. Maynilad and Manila Water were also given the authority to collect fees directly from consumers in exchange for their services. However, any rate increase would need to be approved by the MWSS. Maynilad and Manila Water petitioned for a rate increase in 2013. In computing the new rate, the two companies treated corporate income taxes as a business expense to be passed on to consumers. The relevant petitions were denied by the MWSS. Maynilad and Manila Water then separately submitted their disputes to arbitration, *i.e.*, the Maynilad arbitration and the Manila Water arbitration.

In the Manila Water arbitration, it was decided that Manila Water could not increase its water rates by tacking on its corporate income taxes in the computation of its rates. In the Maynilad arbitration, the arbitral award allowed Maynilad to include the corporate income taxes in the computation of its water rates and, thereby, allowed it to charge higher rates for its services.

## Arbitrability

The Court ruled that the disputes submitted to arbitration by the two concessionaires on rate adjustment are arbitrable. In reaching this conclusion, the Court looked at Section 6 of the [Alternative Dispute Resolution Act of 2004](#), which specifies types of disputes that cannot be resolved through arbitration or other alternative means of dispute resolution. These are: (1) labor disputes covered by the Labor Code of the Philippines, (2) the civil status of persons, (3) the validity of a marriage, (4) any ground for legal separation, (5) the jurisdiction of courts, (6) future legitime, (7) criminal liability, and (8) those dispute subject matters which under the Civil Code of the Philippines cannot be compromised. As the propriety of water rate adjustments does not fall under any of the eight categories, the Court ruled that the disputes were properly submitted to arbitration.

## Public Policy

The Court refused to enforce the arbitral award obtained by Maynilad on the basis that it is against public policy to do so. Citing *Mabuhay Holdings Corporation v. Sembcorp Logistics Limited* (discussed [here](#)), the Court noted that it takes a narrow and restrictive approach when dealing with the public policy exception. Mere errors in the interpretation of the law or factual findings would not be enough to refuse enforcement under the public policy ground. Rather, arbitral awards that are deemed “contrary to public policy are those that, when enforced, would be against Our State’s fundamental tenets of justice and morality, or would blatantly be injurious to the public, or the interests of society.”

The Court concluded that the Maynilad arbitral award was contrary to public policy as it allowed the company to include corporate income taxes in the computation of its water rates. The Court classified Maynilad as a public utility and found that it could not, therefore, pass on to consumers its corporate income taxes. The Court held that enforcing the award would “adversely affect the public at large, specifically, the water consumers in Service Area West served by Maynilad.” Apart from being injurious to the public, the Court stated that it also could not enforce the award as doing so would result in an unequal treatment of water consumers in the Service Area East under Manila Water and in the Service Area West under Maynilad.

It bears noting that the Court also confirmed in obiter that the Maynilad arbitral award would be “illegal.” The Court reasoned that, under Republic Act No. 6234, the MWSS has the power to periodically fix water rates and sewerage services fees as it may deem just and equitable. Thus, only the MWSS has such power, and a court would be exceeding the scope of its power by confirming the Maynilad award.

## Analysis

This decision clarifies what is and what is not arbitrable under Philippine law and jurisprudence. In emphasizing party autonomy, the Court found that so long as a dispute is not among the eight categories mentioned above, the dispute is arbitrable. Here, the dispute was deemed suitable for

arbitration as it revolved around the propriety of water rate adjustments. However, after finding that enforcing the resulting arbitral award would be injurious to the public and would result in unequal protection between water consumers under Maynilad and Manila Water, the Court refused to enforce the same on the ground that it would be against public policy to do so.

The ruling affirms that any dispute between Philippine government entities, including government corporations, and private companies arising from commercial agreements or even concession agreements imbued with public interest are arbitrable. But the ruling also seems to imply that while a dispute based on a concession agreement over rate adjustments for services offered to the public, such as water services or toll road fees, is arbitrable, any award obtained will be considered illegal under Philippine law if there already exists a government entity mandated to determine and fix the rates.

This decision may prove to be problematic. It is possible for parties, including government entities, to commence arbitration proceedings for completely arbitrable disputes only to have the resulting arbitral award declared illegal. Not only that, if the award is deemed to adversely affect the public, enforcement may also be refused on the ground that it is violative of public policy. There are several contracts involving government entities containing arbitration clauses. Following *Maynilad*, parties may need to establish an additional layer of scrutiny to determine whether a dispute is worth resolving via arbitration even when it is technically arbitrable. Even if arbitration is an option, it might not be the most appropriate course of action given the regulatory framework in the Philippines. It would be prudent for parties to consider existing laws and regulations that may render any eventual arbitral award unenforceable. Parties can survey legislation or rules to determine if there exists a clear, explicit, well-defined public policy, one that is “[directly ascertainable by reference to a statute, implementing administrative rules and court decisions and not merely from ambiguous and murky general considerations of supposed public interests.](#)” For policymakers, reconciling the definition of arbitrability with the concept of public interest will offer better clarity for parties who may consider arbitration.

## Conclusion

The *Maynilad* ruling is a welcome decision as it affirms party autonomy and sheds light on what is considered arbitrable under Philippine law. It enriches Philippine jurisprudence relating to both domestic and international arbitration. But, on the other hand, parties may now need to think twice before spending valuable resources in commencing an arbitration for disputes arising from commercial contracts or concession agreements with government entities. While such disputes are arbitrable, an arbitral award obtained may be invalidated under Philippine law and refused enforcement under the public policy exception.

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