

The Proper Law of the Arbitration Agreement – Express Choice makes a come-back?

I have previously written extensively on the question of the proper law of an arbitration agreement¹ where I concluded that absent express choice, any implied choice or closest and most real connection ought to be with the system of law at the seat rather than the governing law of the host or matrix contract². There were several principled reasons for this essentially drawing on the need for international consistency. Those national laws³ that address the issue provide that in the absence of express choice the law of the agreement to arbitrate is to be that of the seat. Those institutional rules⁴ that address the same issue arrive at the same result.

I argue that there ought to be a common international solution to an international problem. The NYC (and to a lesser degree, the Model Law) point towards the conclusion that the courts where the challenge to an award is made, at the seat, ought logically to apply, absent express choice to the contrary, the laws of that nation. If any implication is to be drawn, then in light of the Model Law, NYC and orthodox private international law, the implication should favour the “seat” theory rather than the “host contract” theory. It will also be recalled that those cases that have reached the Supreme Court have proceeded on the basis of the law of the seat being the law of the agreement to arbitrate, seemingly without objection, and perhaps even endorsement by Lord Collins in *Dallah*⁵.

Interestingly, the focus of the English jurisprudence has moved to considering express choice (whether that is a desire to avoid the quagmire of implied choice and closest and most real connection, is moot). In the event that there is an express choice, that is “conclusive”: *R. v International Trustee*⁶ and “where there is an express statement by the parties of their intention to select the law of the contract, it is difficult to see what qualifications are possible, provided the intention expressed is bona fide and legal, and provided there is no reason for avoiding the choice on the ground of public policy”: *Vita Food Products Inc v Unus Shipping Co Inc.*⁷. Where a seat of arbitration is specified and no choice of law for the contract generally is otherwise conveyed by its terms, the choice of seat may convey or imply a choice of law for the contract as a whole: see, for example, *Compagnie d'Armement Maritime SA v Compagnie Tunisienne de Navigation*⁸.

¹ Arbitration (2019) Vol 85 Issue 3, The Law of the Arbitration Agreement: The English Courts Decide? American Review of International Arbitration – 2013 / Volume 24 No. 3

² That is to say the contract within which the agreement to arbitrate is typically a clause.

³ Scotland and Sweden

⁴ The LCIA Rules (2014) Art.16.4 and LMAA Terms (2017) Art. 6 (assuming LMAA to be an institution for these purposes).

⁵ *Dallah Real Estate and Tourism Holding Co v Ministry of Religious Affairs of the Government of Pakistan* [2010] UKSC 46, [2011] 1 AC 763.

⁶ [1937] AC 500 at 529, [1937] 2 All ER 164

⁷ [1939] AC 277 at 12, [1939] 1 All ER 513

⁸ [1971] AC 572

In neither of the landmark cases in the Court of Appeal (*C v D*⁹ and *Sulamérica*¹⁰) was it considered that there was an express choice of the law governing the agreement to arbitrate. The modern tendency to look at express choice can be traced back to the decision in *Arsanovia*¹¹. Andrew Smith J thought it would have been open to submit that there was an express choice (although neither party did make that submission). His reasoning was that the governing law clause provided that ‘*This agreement*’ was governed by Indian law. *C v D* and *Sulamérica* had clauses referring to ‘*the*’ or ‘*this*’ ‘*policy*.’ Andrew Smith J reasoned that the reference to ‘*policy*’ was more naturally related only to the insurance aspects rather than the agreement as a whole and the reference to the ‘*agreement*’ was apt to include all clauses in the ‘host’ contract including the agreement to arbitrate.¹² Andrew Smith J’s construction of ‘*agreement*’ against ‘*policy*’ is, I suggest, a “*fussy distinction*” of a kind deprecated in *Fiona Trust v Privalov*¹³ but it seems to have some traction. It remains better to have clearer words that refer to the host contract, at the very least, and preferably specifically the agreement to arbitrate being subject to a system of law and that is usually done by reference to words such as “*governed by*” “*to be construed in accordance with*” or “*subject to*.”

The two most recent cases considering express choice are *Enka Insaat ve Sanayi A.S v OOO "Insurance Company Chubb", Chubb Russia Investments Limited, Chubb European Group Se, Chubb Limited*¹⁴ (“Chubb”) and *Kabab-Ji S.A.L. (Lebanon) v Kout Food Group (Kuwait)*¹⁵ (“Kout Foods”).

In Chubb, Chubb prevailed in a trial of a claim for injunctive and declaratory relief in a claim brought by Enka, a Turkish engineering company involved in the construction of a power plant in Russia. Following a catastrophic fire at the plant in February 2016, which caused approximately US\$400m-worth of damage, Chubb Russia paid an insurance claim made by the owner and was subrogated to the owner’s rights against Enka. In May 2019, Chubb Russia commenced proceedings against Enka and ten other defendants in Moscow.

In September 2019, Enka brought a claim in England for anti-suit injunctions and related relief against Chubb for breaching a London arbitration clause contained in the construction contract between Enka and Chubb’s insured (the “Construction Contract”). It was common ground between the parties that the arbitration agreement was valid and binding on Chubb but Chubb denied that the Moscow proceedings were within the scope of the agreement. At the same time, Enka applied to the Moscow Court to stay those proceedings pursuant to the New York Convention.

Chubb argued that both the Construction Contract and the arbitration agreement contained within it were governed by Russian law, with the result that the English Court was not the appropriate forum to determine whether there had been a breach of the arbitration agreement – at least in circumstances where there was a good arguable case that the Russian proceedings did not fall within the scope of the arbitration agreement as a matter of Russian law, and those proceedings were being pursued in good faith. By contrast, Enka argued that the arbitration agreement was governed by English law and that the Russian proceedings were a breach of the agreement under English law, so that an injunction should be granted on *Angelic Grace* principles.

⁹ *C v D* [2007] EWCA Civ 1282, [2008] 1 All ER (Comm) 1001.

¹⁰ *Sulamérica Cia Nacional de Seguros SA v Enesa Engenharia SA* [2012] EWCA Civ 638

¹¹ *Arsanovia Ltd v Cruz City 1 Mauritius Holdings* [2012] EWHC 3702 (Comm), [2013] 2 All ER (Comm) 1.

¹² This view derives some support from *ABB Lummus Global Ltd v Keppel Fels Ltd* [1999] 2 Lloyd’s Rep 24 at 35: “A better view seems to me to be that ... the parties agreed that the whole contract, including the arbitration agreement, should be governed by ... English law. Thus, the proper law of the whole contract, including the arbitration agreement, was English law. However, this is not a finally concluded view and may, indeed, be a matter for the arbitrators.” And see *Union of India v McDonnell Douglas* [1993] 2 Lloyd’s Rep 48.

¹³ *Fiona Trust v Privalov* [2007] UKHL 40 at [27].

¹⁴ [2019] EWHC 3568 (Comm). There is an appeal pending against the decision of Andrew Baker J.

¹⁵ [2020] EWCA Civ 6

Andrew Baker J agreed with Chubb that the English Court was not the appropriate forum to determine whether there had been a breach of the London arbitration agreement. If Enka was not content with pursuing its application before the Moscow Court to stay the claim against it to arbitration, then Enka should have commenced arbitral proceedings and sought relief from the arbitrators. The Judge commented that, in normal circumstances, an anti-suit injunction defendant who challenges the appropriateness of the English Courts for the resolution of the issues raised against him should make a *forum non conveniens* application to stay or set aside the claim pursuant to CPR Part 11, or else he will be left to fight his corner at trial on the questions of breach and 'strong reasons'. The unusual procedural history of this particular case took it outside the norm, however, such that Enka's failure to refer the matter to arbitration remained a relevant consideration weighing in the Chubb's favour.

Although Andrew Baker J did not actually decide the choice of law issues, his judgment also contains a timely analysis of the caselaw on the proper law of arbitration agreements. The Judge observed that "*there are choices of seat and choices of seat*": in other words, not all choices are equal, and a choice of seat is not always sufficient to convey a choice of law for the arbitration agreement that is different from the choice of law for the contract as a whole.

Andrew Baker J recited that it was trite law as follows:

- a. In principle, different parts of a single contract may be governed by different systems of law.*
- b. The separability of an arbitration agreement makes it a natural candidate for at least the possibility that it might be governed by a system of law different to that which governs the contract generally.*
- c. An express choice of seat may, but need not, convey or imply a choice of governing law for an arbitration clause.*¹⁶

He continued by agreeing with Lord Neuberger MR in *Sulamérica* that "*the proper law of an arbitration agreement ... is a matter of contractual interpretation, so that inevitably " the answer must depend on all the terms of a particular contract, when read in light of the surrounding circumstances and commercial common sense "*."¹⁷

Nevertheless, he continued that he considered it to be "*an error of analysis*" to see *Sulamérica* as a case about whether the express choice of Brazilian law for the insurance policy¹⁸ as a whole meant there was an implied choice of Brazilian law for the arbitration agreement. In saying so he acknowledged that that was exactly how Moore-Bick LJ had articulated his conclusion¹⁹.

He continued that the question that arose was "*the proper construction of clause 7, not a question of implied choice. Looking at clause 7 in isolation, it might naturally be thought that saying " this policy will be governed exclusively by the laws of Brazil " would convey that the meaning and effect of all of the terms of the policy was to be governed by Brazilian law; and the arbitration agreement was one such term, it was clause 12 of the policy.*"²⁰

¹⁶ At [47]

¹⁷ At [50]

¹⁸ It will be recalled that the choice of law clause in *Sulamérica* was clause 7 of the policy and was in these terms: "*Law and jurisdiction It is agreed that this policy will be governed exclusively by the laws of Brazil. Any disputes arising under, out of or in connection with this policy shall be subject to the exclusive jurisdiction of the courts of Brazil.*"

¹⁹ At [31] of *Sulamérica*

²⁰ At [54]

The proper construction of an express contract term does not, of course, stop at what the words of the particular term in question might naturally convey when considered in isolation.

The *Sulamérica* decision, Andrew Baker J reasoned is then is better understood as a decision that, “upon the proper construction of the policy, i.e. considering what reasonable parties in the position of the contracting parties would have understood to be conveyed by the words they used in their contract in the circumstances in which they were contracting, the choice of Brazilian law in clause 7 did not convey after all that clause 12 was governed by Brazilian law.”²¹

The analysis continued that if, as Andrew Baker J suggests, the “*limitation of clause 7 of the policy upon the proper construction of the policy as a whole, namely that it did not extend to clause 12, was a matter of construction, it was surely as much a matter of construing clause 12 as it was of construing clause 7.*” Thus, despite the seemingly unqualified language of clause 7, clause 12 conveyed that it itself was governed by English law. Thus, the decision that the arbitration agreement in *Sulamérica* was governed by English law was better viewed as a matter of choice of governing law upon the proper construction of clause 12, and not as an application of a 'closest and most real connection' test as would be applied if there had been no choice.

In *Kout Food 'J'* was a Lebanese company which had entered into a Franchise Development Agreement (FDA) with a Kuwaiti company (Z). In 2005, Z became a subsidiary of K, another Kuwaiti company. A dispute arose under the FDA, which J referred to arbitration before the ICC in Paris, pursuant to the FDA. It commenced the arbitration only against K, not Z. The arbitrators concluded that the issue of whether K was bound by the arbitration agreement was a matter of French law, but the issue of whether a transfer of substantive rights and obligations had taken place was governed by English law. They concluded that, as a matter of English law, a 'novation' was to be inferred by the conduct of the parties adding K as the main franchisee, and that K was in breach of the FDA. K filed an annulment application before the French courts. In the meantime, J issued proceedings in England under the Arbitration Act 1996 s.101 and the English court made an *ex parte* order for the award to be enforced as a judgment. K applied for an order that recognition and enforcement of the award as a judgment be refused and for the setting aside of the *ex parte* order. The court ordered the trial of certain preliminary issues, during which the judge found that English law governed the validity of the arbitration clause and the issue of whether K ever became a party to it. He found that as a matter of English law, K did not become a party to the FDA or, consequently, to the arbitration agreement.

As regards the governing law of arbitration agreement the Court of Appeal held that the FDA included all the terms of agreement, including the arbitration clause, and which was governed by and construed in accordance with the laws of England. There was nothing in the argument that the arbitration clause did not contain express words that the arbitration agreement should be governed by English law: a clear intention that the entire FDA was to be governed by English law was demonstrated. That express choice of English law was not affected by the fact that the arbitration clause provided that the seat of the arbitration was to be Paris. The judge was correct that there was an express choice of English law as the govern the arbitration agreement.

²¹ At [55]

Flaux LJ²² held that it was “correct that Articles 1²³ and 15²⁴ of the FDA in themselves provide for the express choice of English law to govern the arbitration agreement in Article 14. Article 1 makes it clear that “This Agreement” (capitalised) includes all the terms of agreement then set out, which include Article 14. Because Article 15 provides that: “This Agreement [again capitalised] shall be governed by and construed in accordance with the laws of England” it is making clear that all the terms of the Agreement, including Article 14, are governed by English law. The answer to the suggestion that, if this analysis were correct, there would be an express choice of governing law of the arbitration clause in every contract which contains a governing law clause is essentially that given by Andrew Smith J in *Arsanovia* at [22]²⁵. Governing law clauses do not necessarily cover the arbitration agreement. This one does because of the correct construction of the terms of Articles 1 and 15 taken together.”²⁶

Flaux LJ continued: “the terms of Article 14 [the agreement to arbitrate] itself do not militate against the conclusion that the governing law provision in Article 15 also encompasses the arbitration agreement in Article 14. On the contrary, ..., the first sentence of Article 14.³²⁷ supports the conclusion that, on the true construction of the FDA as a whole, there is an express choice of English law to govern the arbitration agreement. ... In my judgment, that means that the arbitrators must apply all the provisions, including the governing law clause in Article 15, ...”

Before leaving the judgment in *Kout Foods*, there are, to me, a couple of strange paragraphs²⁸ which appear to discuss whether an implied choice, is either the same as an implied term, or at least is to be decided on the same manner as to whether there is an implied term.

As Flaux LJ correctly points out the test for the implication of a term is now the *Marks and Spencer*²⁹ test. In that case Lord Neuberger said that “Lord Hoffmann suggested [in *Belize Telecom*] that the process of implying terms into a contract was part of the exercise of the construction, ...”³⁰. That is not correct, as Lord Neuberger explained: “I accept that both (i) construing the words which the parties have used in their contract and (ii) implying terms into the contract, involve determining the scope and meaning of the contract. However, Lord Hoffmann’s analysis in *Belize Telecom* could obscure the fact that construing the words used and implying additional words are different processes

²² With whom Sir Bernard Rix and McCombe LJ agreed.

²³ Art 1 provided: “This Agreement consists of the foregoing paragraphs, the terms of agreement set forth herein below, the documents stated in it, and any effective Exhibit(s), Schedule(s) or Amendment(s) to the Agreement or to its attachments which shall be signed later on by both Parties. It shall be construed as a whole and each of the documents mentioned is to be regarded as an integral part of this Agreement and shall be interpreted as complementing the others.”

²⁴ Art 15 provided: “This Agreement shall be governed by and construed in accordance with the laws of England.”

²⁵ The relevant passage Flaux LJ presumably had in mind was: “When the parties expressly chose that “This Agreement” should be governed by and construed in accordance with the laws of India, they might be thought to have meant that Indian law should govern and determine the construction of all the clauses in the agreement which they signed including the arbitration agreement. Express terms do not stipulate only what is absolutely and unambiguously explicit, and it seems to me strongly arguable that that is the ordinary and natural meaning of the parties’ express words (notwithstanding relatively recent developments in the English law about the separability of arbitration agreements from the substantive contract in which it was made and assuming that these foreign companies are to be taken to have known about the developments in 2008 when they concluded the SHA).”

²⁶ At [62]

²⁷ That first sentence provided: “The arbitrator(s) shall apply the provisions contained in the Agreement.”

²⁸ At [53] and [54]

²⁹ *Marks & Spencer Plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72

³⁰ At [22]

*governed by different rules.*³¹ Whether the parties have impliedly chosen a system of law is a question of construction, as demonstrated above, not least by Lord Neuberger MR in *Sulamérica*. Implied terms are governed by a different process and rules. In so far as Flaux LJ suggested otherwise, I suggest he has fallen into error.

Kout Foods may well balance the well-established principle of the separability of arbitration agreements with the common-sense acknowledgment that those agreements most often sit within 'host' contracts with which they are read as a whole. Where there is a clear intention that the two be construed together and where there is no indication in the arbitration agreement that it was intended to be interpreted in isolation, the principle of separability will not insulate the arbitration agreement from construction alongside its 'host'. On its facts and the, perhaps unusual, capitalisation of words, it is a defensible decision. But the broad endorsement of Andrew Smith J in *Arsanovia* is more troubling: he was influenced by whether the noun was agreement or policy. I suggest it will be a rare case that as a matter of construction, the simple juxtaposition of clauses in a composite document called an agreement, is sufficient.

It is clear from these decisions that there is a greater tendency to consider an express choice, something that was rather overlooked in the *CvD* versus *Sulamérica* debate: perhaps even by me!



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³¹ At [26]. And see at [27]: “Of course, it is fair to say that the factors to be taken into account on an issue of construction, namely the words used in the contract, the surrounding circumstances known to both parties at the time of the contract, commercial common sense, and the reasonable reader or reasonable parties, are also taken into account on an issue of implication. However, that does not mean that the exercise of implication should be properly classified as part of the exercise of interpretation, let alone that it should be carried out at the same time as interpretation. When one is implying a term or a phrase, one is not construing words, as the words to be implied are *ex hypothesis* not there to be construed; and to speak of construing the contract as a whole, including the implied terms, is not helpful, not least because it begs the question as to what construction actually means in this context.”