ENKA V. CHUBB – DEMYSTIFYING THE PERPLEXING ISSUE OF THE PROPER LAW OF ARBITRATION AGREEMENT

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Introduction

International arbitration is distinct from domestic arbitration basically because national arbitration is subject to a particular domestic law. In contrast, international arbitration is not subjected to one unless parties, by their agreement, choose a national law to govern different aspects of their disputes. The agreement of arbitration, generally a part of the main contract, is different in its nature from the main contract. This aspect has been recognised early enough, for example, in *Heyman v. Darwin Ltd.*[1] where the distinction was made solely to emphasise on the fact that a breach of the liabilities and obligations under the main contract may lead to the termination of the main contract, but cannot lead to the end of the arbitration agreement Indeed, the arbitration agreement, which is remedial in nature, would come into the picture when disputes arise under the main contract. So, an arbitration agreement does not create nights and obligations of its own but provides a means to settle the disputes which arise out of the rights and obligations provided in the main contract. Hence, the question arises as to what law shall govern the arbitration agreement to achieve the end result.

However, parties seldom choose the governing law of the arbitration agreement. This has frequently given use to complexities. The simplest and most obvious solution, but one that is not yet established for some reason, it for arbitration clauses to make an explicit choice of the law applicable to that particular clause itself rather than to the matrix contract of which the clause is one small element. The recent decision of the United Kingdom (UK) Supreme Court (SC) in *Enka Insaat Ve Sanayi AS v. 000 Insurance Company Chub*[2] (Enka v. Chubb) has been successful in providing some much-needed clarity regarding this. It has addressed the principles for ascertaining the proper law of an arbitration agreement.

[1] *Heyman v. Darwin Ltd* [1942] A.G 356.
[2] *Enka Insaat Ve Sanayi AS v. 000 Insurance Company Chub* [2020] UKSC 38 (hereinafter 'SC Enka').

Enka v. Chubb

In 2012, in relation to the construction of the Berezovskaya power plant in Russia, the claimant, Enka, agreed to provide certain services. A fire mishap occurred at the plant in February 2016. The defendant insurer, Chubb, claimed to have paid $ 400 million to the owner of the plant with respect to the damage caused due to the accident. In September 2019, Chubb commenced proceedings in the Moscow Arbitration Court against 11 parties, including Enka, where it alleged that Enka and the rest caused the fire. The contract of Enka contained an arbitration agreement providing for arbitration at the International Chamber of Commerce (ICC) in London. Accordingly, Enka issued a claim in the commercial court for an anti-suit injunction in order to restrain Chubb from going ahead with the Russian proceedings. Chubb opposed this claim by arguing that the law governing the arbitration agreement is Russian law and that the Russian proceedings did not fall within the scope of it, although it was common ground that they did if English law was the proper law.

The claim was dismissed at trial on the ground that the English court is not the *forum conveniens* to address this. When appealed, the Court of Appeal[3] noted that there are two ways to approach the issue of the governing law of the arbitration agreement. On the one hand, there are those who say that the law that governs a contract should generally also govern an arbitration agreement which, though separable, forms part of that contract. This approach was previously taken by the court of appeal in *Sulamérica Cia Nacional de Seguros SA v. Enesa Engenharia SA*[4] (Sulamerica). On the other hand, there are those who say that the law of the chosen seat of the arbitration should also generally govern the arbitration agreement, as noted in *C v. D*.[5] The court of appeals found the decision of Sulamerica to be inconsistent with the decision in *C v. D* decision and upheld the decision as given in the latter case by observing that, "*until and unless there has been an express choice of the law that is to govern the arbitration agreement, the general rule should be that the arbitration agreement is governed by the law of the seat, as a matter of implied choice. subject only to any particular features of the case demonstrating powerful reasons to the contrary*".[6]

The decision of the Court of Appeals was appealed in the SC. The bone of contention of this appeal concerned what system of national law governs the validity and scope of the arbitration

[3] *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb* [2020] EWCA Civ 574 (hereinafter EWCA Enka).
[4] *Sulamérica Cia Nacional de Seguros SA v Enesa Engenharia SA* [2012] EWCA Civ 638 (hereinafter "Sulamerica").
[5] *C v D* [2007] EWCA Civ 1282.
[6] *EWCA* Enka (n 3) 90.

agreement when the law applicable to the arbitration seat differs from the law applicable to the contract.

Decision of the Supreme Court

Although the SC reached the same outcome as the Court of Appeals, it departed from the approach taken by the lower court. The SC decided that where there has been no choice of law to govern the arbitration agreement, but a choice has been made as to the law governing the contractual agreement, that choice will also generally apply to the arbitration agreement. However, when the parties have not chosen impliedly or explicitly any law to govern the contract, the proper law would be the one closely connected, and that being the law of the seat of arbitration. To come to this conclusion, the majority reasoned as follows.

Where a court of the UK or Wales has to decide the choice of law for a contract, Rome I regulations[7] are applied. However, as mentioned in Article 1(2)(e) of the Rome I regulation,[8] arbitration agreements are excluded from its scope. Hence to determine the proper law, the common law rules have to be applied. The common law rules entail a three-stage test to determine the governing law, where *firstly*, it is to be determined whether the parties have made an express choice of law for the arbitration agreement; *Secondly*, in the absence of an express choice, the court has to determine whether there is an implied choice of law; and *thirdly*, in the absence of both express and implied choice, the court has to find as to with which law is the contract "most closely connected".[9]

Express choice of law

The SC did not endorse the strict application of the doctrine of separability, which the Court of Appeals applied to hold otherwise. The doctrine of separability provides that an international arbitration agreement is separable from the underlying instrument with which it is associated.[10] The consequence of this principle is for the parties' arbitration agreement to be governed by a law different from the law governing their main contract.[11]

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[7] Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) [2008] OJ L177/6.
[8] Ibid Article 1(2)(e).
[9] Dicey, Morris & Collins, *The Conflict of Laws*, (15th edn., Sweet & Maxwell 2012) rule 64(1) (hereinafter Dicey & Morris); *SC Enka* (n 1) 27.
[10] Gary Born, *International Commercial Arbitration* (2nd edn, Kluwer Law International 2014) 464 (hereinafter G Born).
[11] Sulamerica (n 4) 11.

The majority observed that where there is no express choice of law applicable to the arbitration agreement, but a law has been chosen to govern the contract, such law governing the contract will also be the law which shall govern the arbitration agreement. The reason is the arbitration agreement being a part of the contract, would also be subjected to the law applicable to the contract as the governing law clause of the contract begins with the words "This agreement", which means that the chosen law to govern the contract shall also govern the arbitration agreement unless good reasons are provided to the contrary. Since the arbitration clause is only one of many clauses in a contract, it might seem reasonable to assume that the law chosen by the parties to govern the contract will also govern the arbitration clause. In holding as such, the majority relied on similar reasoning as provided by many commentators on International Arbitration[12] and also upheld a recent decision of the Court of Appeals *in Kabab-Ji SAL (Lebanon) v Kout Food Group (Kuwait)*[13], where a similar choice of law clause of the contract was construed as to govern and determine the construction of all the clauses in the agreement which they signed including the arbitration agreement. The court further stated that it has to be construed in this manner as the law applicable to the underlying contract provides for a greater degree of consistency and legal certainty and also assists in avoiding the artificiality of such a strict application.[14]

Implied choice of law

The Court of Appeals held that there is a strong presumption that in the absence of an express choice of law, the procedural law of the seat is the implied choice to govern the arbitration agreement.[15] The court relied upon the "overlap principle" and observed that there exists a considerable overlap in the provisions of the Arbitration Act 1996[16] (1996 Act) and the arbitration agreement. It opined that in such situations, one generally expects the parties to intend the same law to govern both the procedural law of the seat and the substantive law of the arbitration agreement.

The SC overruled this position, noting that the governing law of the arbitration process is conceptually distinct from the law which governs the validity and scope of the arbitration

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[12] *G Born* (n 10) 592; Grover, Dilemma of the Proper Law of the Arbitration Agreement: An Approach Towards Unification of Applicable Laws' (2014) Sing. L. Rev. 227, 255; Choi, 'Choice of Law Rules Applicable for International Arbitration Agreements' (2015) Asian International Arbitration Journal 105, 108-109; Bantekas, The Proper Law of the Arbitration Clause: A Challenge to the Prevailing Orthodoxy' (2010) Journal of International Arbitration 1, 1-2.

[13] [2020] EWCA Civ 6.

[14] *SC Enka* (n 1) 53; *Dicey & Morris* (n 9) paras 12-103 and 12-109.

[15] *SC Enka* (n 1) 91.

[16] Arbitration Act 1996 (UK).

agreement. The reason is almost all the provisions of the 1996 Act relied by the Court of Appeals to support the overlap argument are non-mandatory and, where the arbitration agreement is governed by a foreign law, by reason of section 4(5) of the 1996 Act,[17] the non-mandatory provisions of the Act which concern arbitration agreements do not apply to it.[18] The SC was right in observing that in such events, inferences cannot be drawn that, by choosing English law as the law of the seat, parties were also impliedly choosing English law to govern their arbitration agreement.

However, the majority did reaffirm the 'invalidity principle' as propounded in *Sulamerica*, as a choice of an arbitral seat may be considered as an implied choice of governing law of the arbitration agreement in situations where the arbitration agreement would be unenforceable or invalid under the per which law governing the underlying contract.[19] The ratio behind this principle, as the majority held, is that an interpretation that upholds a transaction's validity is to be preferred to one that would render it invalid or ineffective. Hence, the law of the seat can also govern the arbitration agreement where there exists any provision of the law of the seat which shows that, where an arbitration is subject to that law, the arbitration will also be treated as governed by that country's law.[20]

Closely connected law

In cases where it is impossible to ascertain the explicit or implicit choice of law, it becomes imperative that the law closely connected to the agreement be applied. In these circumstances, the closely connected law must determine objectively and irrespective of the parties' intention. The application of this rule is interesting as it is different in nature from the attempt to identify a choice (express or implied), as this involves the application of a Rule of law and not any process of contractual interpretation.

Based on this, the majority and one of the minority judges came to the conclusion that the law of the seat would be closely connected to the arbitration agreement.[21] The reasons were many. *Firstly*, t approach reflected the status of the seat as the place where the arbitration was to be performed legally and to which the parties submit themselves for the purpose of resolving any issue related

[17] Ibid s 4(5).
[18] *SC Enka* (n 1) 73.
[19] *SC Enka* (n 1) 109.
[20] *SC Enka* (n 1) 170 (vi).
[21] *SC Enka* (n 1) 118-120; *Sulamerica* (n 4) 32; *Dicey & Morris* (n 9) rule 64(1)(b) and para 16-016; David St. John Sutton, Francis Russell & Judith Gill, Russell on Arbitration, (24th edn., Sweet & Maxwell 2015) 2-121.

to the validity or enforceability of their arbitration agreement[22]; *Secondly*, this approach is in consonance with what is followed and widely practised in international law,[23] especially Article V(1)(a) of the New York Convention;[24] *Thirdly*, Such an application upholds the reasonable expectation of the contracting parties who without choosing the governing law of the arbitration agreement, choose a place of arbitration[25]; and *lastly*, this gives the required legal certainty by allowing the contracting parties to predict easily as to, in the absence of party choice, what would be the governing law.[26]

Applying these reasonings to the facts, the majority and a minority judge, out of the dissenting judges, concluded that neither an explicit nor an implicit choice of law existed to govern their arbitration agreement. Accordingly, applying the *closest and most real connection test*, it was found that the arbitration agreement was governed by English law, i.e., the law of the seat and not governed by Russian Law.

Conclusion

The SC, in this decision, has taken a major step in clearing the air around a much-debated issue of the governing law of the arbitration agreement. The court has been thoughtful in considering the commercial purpose of the party as one of the reasons while applying the close connection test to conclude that the law governing the seat shall be the proper law since, in the end, a party chooses a seat which is considerate and supportive of arbitration. As the distinguished jurist Gary Born puts it, in most jurisdictions, national law provides that international arbitration agreements should be interpreted in light of a 'pro-arbitration' presumption.[27]

In essence, the court affirmed the previous choice of law approach of *Sulamerica*, clarifying the issue While doing so, it applied numerous international authorities to support its position, further strengthening this position and providing certainty of outcome. The court systematically interpreted the New York convention, which has already been signed by around 160 countries and aims at establishing a uniform set of international legal standards for recognising and enforcing arbitration agreements and awards. Its success is reflected by the implementation of the same by

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[22] *SC Enka* (n 1) 121-124; *Minister of Finance (Inc) v International Petroleum Investment Co* [2019] EWCA Civ 2080, 36-49; *Sulamerica* (n 4) 104.
[23] *SC Enka* (n 1) 125-141.
[24] Convention on the Recognition and Enforcement of Foreign Arbitral Awards (adopted 10 June 1958, entered into force 7 June 1959) 330 UNTS 3, Article V(1)(a).
[25] *SC Enka* (n 1) 142-143.
[26] *SC Enka* (n 1) 144-145.
[27] *G Born* (n 10) 1403.

different domestic legislations and has gained support from some of the leading international arbitration jurists like Gary Born, *van den Berg*, etc. Hence, this stance of the court shall be considered a positive move towards achieving the goal of the international convention.

Considering that the majority decision will be the current binding law, much thought and diligence have to be given before drafting arbitration agreements, and the implications of not choosing a proper law to govern the same have to be well considered.

At the same time, since the SC was divided in its judgment, this may result in a continuation of the debate among arbitration professionals and commentators as to whether the majority's decision was right. There is enough scope for the law to develop as per what the minority has held - (i) that the law governing the main contact, even in the absence of a choice of law provision, should tentatively also apply to the arbitration agreement; or (ii) that in fact, an arbitration agreement is most closely connected with the governing law of the contact.