High Court considers governing law of arbitration agreement and enforcement against non-parties

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AUTHORS

Marie Berard

Benjamin Barrat

Introduction

In *J (Lebanon) v K (Kuwait)*(1) the High Court granted an application for the adjournment of an arbitral award, pending the outcome of a challenge before the Paris Court of Appeal by a non-party to the arbitration agreement.

The arbitration agreement provided for Paris-seated arbitration and was contained in an underlying contract governed by English law. This, the judge held, amounted to an express choice of English law as governing the arbitration agreement. The judgment provides a helpful review of the authorities on whether, in the absence of an express provision, an arbitration agreement is governed by the law of the underlying agreement or that of the seat of arbitration. Another key issue was whether the parties had given effective consent to the joinder of a third party in accordance with the contract's express provisions on variations. In this case, the judge found that the parties' conduct was insufficient to indicate consent.

Background

Section 103 of the Arbitration Act 1996 broadly enshrines Article (V)(1) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the New York Convention). Section 103 sets out circumstances in which the recognition or enforcement of an award made in a New York Convention state may be refused.

In particular, Section 103(2)(b), mirroring Article V(1)(a), allows a court to refuse enforcement of an arbitral award if the person against whom enforcement is sought proves that the arbitration agreement was invalid under the law to which the parties have subjected it.

Under Section 103(5), where an application for the setting aside or suspension of an award has been made to a court of the country in which, or under the law of which, the award was made, the English court may adjourn a decision on the recognition or enforcement of the award.

Facts

The dispute in *J v K* concerned a franchise development agreement (FDA) entered into between J and Z in 2001 in respect of licences to market, prepare and sell food products. Article 14 of the FDA was an International Chamber of Commerce arbitration agreement, providing for arbitration seated in Paris. Article 15 stated that the FDA would be governed by English law. The arbitration agreement itself did not make a reference to governing law.

K subsequently became the holding company of Z. At the time, J consented in writing to the restructuring.

In the arbitration, the tribunal was asked to determine whether K had become a party to the FDA and the arbitration agreement. A majority of the tribunal held that:

- the issue of whether K was bound by the arbitration agreement was a matter of French law, as the validity of the award was contingent upon the law of the seat; and
- under English law, K had become a party to the arbitration agreement by way of novation to be inferred by conduct.

In February 2019 Justice Popplewell granted an *ex parte* order for the enforcement of the award under Section 103 of the Arbitration Act.

K commenced a challenge to the award before the Paris Court of Appeal, with a hearing convened for February 2020. J took the unusual step (as award creditor) of seeking an adjournment of enforcement in England, as well as security for the award amount, under Section 103(5). K made a cross-application for the enforcement order to be set aside.

Decision

Sir Michael Burton, sitting as a judge of the High Court, adjourned the enforcement of the award, pending resolution of the challenge before the Paris Court of Appeal. In reaching his decision, the judge determined the following four preliminary issues:

Does the law governing the validity of the arbitration agreement also govern whether the defendant (K) became a party to the arbitration agreement?
Dallah Real Estate v The Ministry of Religious Affairs(2) and *Dardana Ltd v Yukos Oil Co*(3) clarify that the question of whether K was a party to the arbitration agreement must be determined in accordance with Section 103(2)(b) of the Arbitration Act. Under that section, the law governing the arbitration agreement would be applied to determine whether K became a party.

What is that law?
The judge concluded that, applying Section 103(2)(b), English law had been expressly chosen by the parties to govern the validity of the arbitration clause and whether K was a party to the arbitration agreement.

The judge referenced a number of authorities on the law applicable to an arbitration agreement in the absence of an express choice of governing law.

In *Sul America Cia Nacional de Seguros SA v Enesa Engenharia SA*,(4) the court held that it is necessary to consider "the parties' choice of proper law, express or implied, failing which it is necessary to identify the system of law with which the contract has the closest and most real connection".

As to an implied choice of law, the court in *Channel Tunnel Group Ltd v Balfour Beatty Ltd*(5) considered that it would be exceptional for the proper law of the arbitration agreement to be different from an express choice of law for the host contract. In *Sul America*, the court stated that a search for an implied choice of law to govern the arbitration agreement is likely to lead to the conclusion that the parties intended that agreement to be governed by the same law as the substantive contract.(6)

While in *C v D*(7) the court stated that an implied choice of governing law is "more likely to be the law of the seat of the arbitration than the law of the underlying contract", in *BCY v BCZ* (High Court of Singapore)(8) and *Arsanovia Ltd & Ors v Cruz City 1 Mauritius Holdings*,(9) the courts stated that the governing law of the main contract would be a strong indicator of the governing law of the arbitration agreement, in the absence of indications to the contrary.

The judge concluded that, while there would be a "powerful case" for English law as the implied choice of law governing the arbitration agreement, the governing law clause in the underlying agreement (Article 15) amounted to an express choice of governing law applicable to the arbitration agreement.

The arbitration agreement provided that "the arbitrators shall apply the provisions contained in this agreement", being the FDA. Article 1 provided that "[t]his Agreement... shall be considered as a whole", while Article 14(3) provided that "the arbitrators shall also apply principles of law generally recognised in international transactions. The arbitrators may have to take into consideration some mandatory provisions of some countries".

The judge concluded that:

> *It is clear to me that, on the clear construction of Article 14.3, the provisions which the Arbitrators were thus required to apply included the provisions as to law in Article 15, because by Article 14 (3) they must also apply certain other principles of law.*

Under English law, had K become a party to the FDA and, if different, the arbitration agreement?
The judge concluded that, under English law, K had not become a party to either the FDA or the arbitration agreement. While not an argument pursued by the parties, the judge stated that, in theory, there are circumstances in which there could be a difference between the position under the

FDA and the arbitration agreement.

The majority of the tribunal found that K became a party to the FDA by way of a "novation by addition" which, the judge noted, is not a concept recognised by English law. The judge went on to consider whether the parties' conduct had resulted in a joinder of K to the FDA and arbitration agreement and, as such, a variation. That joinder would require the consent (express or implied) of J and Z. J referred to the correspondence by which Z notified J of, and J consented to, the restructuring as evidence that J had consented to K becoming party to the FDA.

The judge did not agree that J's conduct amounted to an implied consent to the joinder of K. The FDA required that:

- J give prior written approval of any assignment or transfer of rights by Z;
- no change, waiver, approval or consent would be binding unless signed by both parties in writing; and
- any amendment or modification to the FDA was to be recorded in a document and signed on behalf of both parties.

These express provisions meant that the parties' conduct was insufficient to join K to the FDA and the arbitration agreement. Burton noted that J had an opportunity to locate further documents, which might support its case that there had been consent to the joinder of K. Therefore, while finding against J on a preliminary basis, the judge left this issue "slightly unanswered".

What was the law governing K's capacity to join the arbitration agreement?
Burton held that Kuwaiti law governed K's capacity to join the arbitration agreement. Article V(1) of the New York Convention and Section 103(2)(a) of the Arbitration Act require a court complying with the New York Convention to look at the personal law of the party said to be under an incapacity.

As to the security application, Burton concluded that J had failed to meet the two requirements set out in *Soleh Boneh International v Uganda and National Housing Corp.*(10) On the merits, the judge concluded that J's chances of enforcing an award in the jurisdiction were "very slim" and that J had failed to adduce any evidence of the need for security or risks if it were not ordered.

Comment

The case provides a cautionary tale of the delays and additional costs that may be incurred if claimants fail to consider closely:

- careful compliance with provisions on variations during the term of a contract; and
- (at the outset of a dispute) which parties should be named as defendants.

The case also highlights the difficulties that may arise if the governing law of an arbitration agreement is ambiguous. The court found that the governing law provision in the underlying agreement amounted to an express choice of law to govern the arbitration clause. Where an arbitration agreement does not contain an express choice of governing law and the law of the seat is different to that governing the underlying contract, it cannot be assumed that the latter will necessarily apply to the arbitration agreement. If the event that the law governing the underlying contract and the law of the seat of arbitration are different, parties should include an express choice of governing law in their arbitration agreement.

For further information on this topic please contact Marie Berard or Benjamin Barrat at Clifford Chance LLP by telephone (+44 20 7006 1000) or email (marie.berard@cliffordchance.com or benjamin.barrat@cliffordchance.com). The Clifford Chance website can be accessed at www.cliffordchance.com.

Endnotes

(1) *J (Lebanon) v K (Kuwait)* [2019] EWHC 899 (Comm).

(2) [2010] UKSC 46, at 104 and 106.

(3) [2002] EWCA Civ 543, at 1.

(4) [2012] EWCA Civ 638, at 9.

(5) [1993] AC 334, at 357 to 358.

(6) *Sul America*, at 26.

(7) [2007] EWCA Civ 1282, at 22.

(8) [2016] SGHC 249, at 65.

(9) [2012] EWHC 3702 (Comm), at 21.

(10) [1993] 2 Lloyd's Rep 208.

Shawn Yap, trainee solicitor, assisted in the preparation of this article.
