International Law Office

ARBITRATION & ADR - UNITED KINGDOM

Supreme Court clarifies principles for determining law of arbitration agreement

22 October 2020 | Contributed by Clifford Chance

AUTHORS

Marie Berard

Eraldo d'Atri

Benjamin Barrat

Introduction

In *Enka Insaat ve Sanayi AS v OOO "Insurance Company Chubb*",(1) the Supreme Court clarified definitively the principles for ascertaining the law governing an arbitration agreement (the AA law). In doing so, the Supreme Court ruled that the Court of Appeal was wrong to find that where the AA law is not expressly specified there is a strong presumption that the parties have, by implication, chosen the law of the seat of the arbitration to be the AA law, or that the law governing the main contract (the main contract law) has little bearing on the AA law. On the contrary, the Supreme Court held that where the AA law is not expressly specified, a choice of main contract law (whether express or implied) will generally also apply to an arbitration agreement which forms part of that contract.

Albeit for different reasons, the Supreme Court ruled that the AA law was English law and thus affirmed the Court of Appeal's decision to grant an anti-suit injunction restraining the defendants from pursuing Russian court proceedings in breach of a London arbitration clause.

Background

It is well established that an arbitration agreement within a contract may be governed by a law different from the main contract law. The determination of the main contract law is governed by the choice of law rules in the EU Rome I Regulation (593/2008). However, since arbitration agreements are expressly excluded from the scope of the regulation, the AA law falls to be determined by traditional common law choice of law rules.

Before *Enka v Chubb* the leading authority, *Sulamerica v Enesa*,(2) set out a three-stage test:

- Have the parties made an express choice of the AA law?
- If not, have they made an implied choice of the AA law?
- If not, with which system of law does the arbitration agreement have its closest and most real connection?

The application of the three-stage inquiry is not always straightforward. The difficulty arises when parties have not made an express choice of the AA law (which is often the case), and the particular circumstances of the case point to different laws as the potential AA law, either a law applicable as a matter of implied choice or the law with the "closest and most real connection". A prime example is when the main contract is governed by one system of law, but the arbitration agreement provides for arbitration seated in a different jurisdiction.

In *Sulamerica* it was held that, in the absence of any indication to the contrary, the AA law would usually follow the main contract law. However, the court in *Sulamerica* also acknowledged that the law of the seat (the 'curial law') may constitute such an "indication to the contrary", although how much significance should be attached to the curial law depends on the circumstances of the case. The choice of the AA law in *Sulamerica* was ultimately resolved in favour of the law of the seat.

Facts

The claimant Enka was a Turkish engineering company with substantial operations in Russia, and the defendants were entities within the Chubb group of insurance companies.

The dispute arose out of the construction of a power plant in Moscow. Unipro, the owner of the plant, engaged Energoproekt as a general contractor, which in turn engaged Enka as a sub-contractor to provide building works in relation to the boiler and auxiliary equipment installation. The contract between Energoproekt and Enka was silent as to the law governing the main contract and contained the following arbitration agreement at Clause 50.1:

> *...If the matter is not resolved within twenty (20) calendar days after the date of the notice referring the matter to appropriate higher management or such later date as may be unanimously agreed upon, the Dispute shall be referred to international arbitration as follows:*
>
> - *the Dispute shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce,*
> - *the Dispute shall be settled by three arbitrators appointed in accordance with these Rules,*
> - *the arbitration shall be conducted in the English language, and*
> - *the place of arbitration shall be London, England.*

Energoproekt subsequently assigned to Unipro all rights against Enka resulting from the contract. The assignment agreement provided that any disputes between Unipro and Enka should be resolved by arbitration in accordance with Clause 50.1 of the contract.

In February 2016 a fire occurred at the power plant. Chubb Russia, Unipro's insurer and the first defendant in this case, made payments to Unipro under the insurance policy and so became subrogated to any rights that Unipro might have against Enka for liability for the fire.

Chubb Russia alleged that the fire was caused by the poor quality of Enka's works and demanded that Enka pay for the losses. Enka asserted that it bore no responsibility for the fire.

In May 2019 Chubb Russia commenced proceedings against Enka (and 10 other parties) in the Moscow courts, claiming damages for the fire which Chubb Russia alleged to have been caused by the poor quality of Enka's works. Enka asserted that Chubb Russia brought this claim in breach of the arbitration agreement at Clause 50.1 of the contract.

In September 2019 the Moscow court accepted to hear Chubb Russia's claim. Enka subsequently issued a claim in the Commercial Court in London, seeking a declaration that Chubb Russia was bound by the arbitration agreement at Clause 50.1 of the contract, and an anti-suit injunction restraining Chubb Russia from continuing the claim before the Moscow courts.

Court of Appeal decision

At first instance, Justice Andrew Baker dismissed Enka's injunction application. Regarding the choice of the AA law, he held that the choice of London as a seat in Clause 50.1 did not indicate a choice of English law as the AA law. While ultimately the judge did not determine the AA law, he held that it was well arguable that the AA law was Russian law.

The Court of Appeal overturned the first-instance decision and granted the anti-suit injunction. The Court of Appeal reached the conclusion that there is a "strong presumption" that where there is no express choice of AA law, the parties have impliedly chosen the curial law to govern the arbitration agreement. In a departure from *Sulamerica*, the court went even further to conclude that the main contract law has little relative weight on the determination of the AA law, and that this general rule was subject only to any particular features of the case demonstrating powerful reasons to the contrary. The Court of Appeal did not elaborate on what these powerful countervailing factors entail, but the main contract law being different from the curial law was not one such factor.

The Court of Appeal also considered there to be sufficient overlap between the scope of powers in the curial law and the substantive arbitration agreement to justify the conclusion that parties who choose England as the seat of arbitration would naturally choose English law as the AA law. This overlap argument was also the main reason why the Court of Appeal found that the curial law, as opposed to the main contract law, would be the law with the closest connection to the arbitration agreement (for further details please see "Court of Appeal clarifies principles for determining law of arbitration agreement").

Supreme Court decision

By a majority of three to two (Lords Hamblen and Leggatt gave the majority judgment, with which Lord Kerr agreed), the Supreme Court dismissed the appeal and affirmed the Court of Appeal's decision that the AA law was that of the seat of arbitration, English law. However, the Supreme Court's reasoning in reaching this

conclusion differed significantly from that of the Court of Appeal.

While the Supreme Court found the Court of Appeal was right to affirm the three-stage test in *Sulamerica*, it reformulated the relative weight to be attached to the curial law where the main contract law and the curial law differ, or where the main contract does not include a choice of law. It held that the correct approach was as follows.

First limb
The court will consider first whether there was an express choice of AA law. This is ascertained by construing the arbitration agreement and the main contract containing it, as a whole, applying the ordinary principles of contractual interpretation of English law.

Second limb
Second, the court will consider whether there was an implied choice of AA law. The Supreme Court reaffirmed the general rule in *Sulamerica* that, where there is a choice of law for the main contract, the parties impliedly chose the main contract law to govern the arbitration agreement as well, unless there is good reason to find otherwise. However, in *Enka* the Supreme Court went further and stated that this general rule applies where there is an implied choice of main contract, as well as an express choice.

Importantly, in a marked contrast to the Court of Appeal, the Supreme Court found that simply because an arbitration clause is to be treated as a distinct agreement for the purposes of determining its validity, existence and effectiveness, it does not follow that the arbitration agreement is regarded as a different and separate agreement for the purpose of determining the AA law.

While the doctrine of separability means that the arbitration clause is more amenable than other parts of a contract to having a different choice of law, the arbitration clause is nonetheless "part of the bundle of rights and obligations" recorded in the main contract. Therefore, the choice of curial law is not, by itself, sufficient to negate the inference that the parties intended the choice of the main contract law to apply to all clauses within the contract, including the arbitration clause.

The Supreme Court set out the following factors that may negate such an inference:

- any provision of the curial law which indicates that, where an arbitration is subject to the curial law, the arbitration will also be treated as governed by that country's law;
- where there is a serious risk that the arbitration agreement would be ineffective if it were governed by the same law as the main contract; or
- where the arbitration agreement contains a standard form clause with distinctive or well-known legal meanings in a different system of law to that of the main contract law.

In *Sulamerica* the overlap argument was provided as one of the two reasons why the parties intended that the curial law (ie, English law) should be the AA law as an exception to the general rule. However, while the Supreme Court agreed that, in principle, a choice of curial law may (based on the content of the relevant curial law) support the finding that the parties intended the law of the seat to govern the arbitration agreement, it disagreed with the reasoning in both *Sulamerica* and the Court of Appeal in *Enka* that, in the case of English law, the content of the Arbitration Act 1996 would lead to such a conclusion. The Supreme Court held that, where there is no choice of law to govern the contract, the provision of a curial law alone is not enough to establish a general rule that the parties impliedly intended the curial law to be the AA law.

Third limb
In the absence of any express or implied choice of AA law, the court must decide with which system of law the arbitration agreement is most closely connected, irrespective of the intentions of the parties.

Citing the leading authorities of *Sulamerica* and *C v D*,(3) the court held that the default rule is that the law most closely connected with the arbitration agreement will be the curial law. The Supreme Court's ruling was based on the following factors:

- the seat is the place of performance of the arbitration agreement;
- consistency with international law (in particular the New York Convention) and legislative policy;
- likelihood to uphold the reasonable expectations of the parties; and
- ability to predict with little argument the law that will apply by default.

The sole exception to this default rule which the court elaborated on was an *obiter* comment that the default rule may not apply where the arbitration agreement would be invalid under the law of the seat, but not under the law governing the rest of the contract.

Conclusion

The court held that the main contract was governed by Russian law due to the close connection of the main contract with Russian law (ie, not because of the parties' choice). The curial law (ie, English law) was held to govern the arbitration agreement also on the basis of the close connection. Therefore, the English courts had jurisdiction to rule on whether the Moscow claim was brought in breach of the arbitration agreement and the Supreme Court affirmed the decision to grant the anti-suit injunction in Enka's favour.

Dissenting opinion

Lords Burrows and Sales disagreed with the majority by holding that the parties had in fact chosen (albeit impliedly) Russian law as the main contract law. In reaching this conclusion, they cited the fact that the contract was written in Russian, made numerous references to Russian law throughout, was to be performed in Russia for a Russian company and that the effects of any breach would be suffered in Russia.

They agreed with the majority judgment's principle that the choice of law (implied or express) for the main contract will also apply to the arbitration agreement where the arbitration agreement is silent. However, they held that if the main contract law had not been impliedly chosen (ie, it had been determined by virtue of the close connection test), Russian law, as opposed to the curial law would have the closest and most real connection with the arbitration agreement. This was because reasonable businesspersons would expect all clauses of the same contract to be coherently governed by the same system of law.

Comment

The Supreme Court's decision in *Enka v Chubb* provides much-needed certainty on the principles that courts should apply to determine the AA law, specifically in cases where there is no express choice and the main contract law differs from the curial law. This is good news not only for international arbitration users at large, but also for London as one of the world's most popular seats.

Although the underlying principles have now been clarified, the weight given by the Supreme Court to an implied choice of the main contract law will mean more uncertainty for the parties in respect of the AA law (where the latter is not expressly chosen). This is likely to result in more disputes, which will only be resolved by the courts on the specific facts of every case.

If anything, the facts and ultimate decision in *Enka* should be a powerful reminder that an arbitration agreement requires attentive drafting. An express governing law choice for both the underlying contract and the arbitration agreement should be included. Failing to draft with sufficient clarity may give rise to lengthy and costly proceedings on procedural issues before any dispute on the merits can be heard.

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

Julia Chobanyan, trainee solicitor, assisted in the preparation of this article.

Endnotes

(1) [2020] UKSC 38.

(2) *Sulamerica Cia Nacional de Seguros SA v Enesa Engelharia SA* [2013] 1 WLR 102.

(3) *C v D* [2007] EWCA Civ 1282.