Dispute Resolution Hotline

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UK SUPREME COURT ON LAW GOVERNING THE ARBITRATION AGREEMENT (ENKA V. CHUBB)

- Where the arbitration agreement does not expressly mention the choice of law governing the arbitration agreement, the choice of law of the main contract will apply to the arbitration agreement;
- Absent an express choice of the governing law of the main contract, the law applicable to the arbitration agreement will have to be determined in accordance with the law that is most closely connected with the arbitration agreement;
- As a general rule, the law of the seat of the arbitration is most closely connected with the arbitration agreement;
- The position of law in India is consistent with the decision of the UK Supreme Court, as set out in NTPC v. Singer (in 1992).

INTRODUCTION

Recently, the Supreme Court of United Kingdom **("UK Supreme Court")** in *Enka Insaat Ve Sanayi AS v. OOO Insurance Company Chubb*,[1] ("**Enka v. Chubb**") has passed a landmark ruling, where they have set out the principles to be followed for determination of the law governing the arbitration agreement. This is the first time the UK Supreme Court has clarified the position of law after a careful consideration of the earlier cases, including the famous decision of the UK Court of Appeal in *Sulamerica v. Enesa Engenharia* ***("Sulamerica")***[2].

The UK Supreme Court has held that where the arbitration clause does not specifically mention the law governing the arbitration agreement, but however mentions the law of the main contract, then the same would normally govern the law governing the arbitration agreement. Where there is no express choice of law governing the main contract, by default, the arbitration agreement would be governed by the law of the seat. The position of law is also consistent with the Indian law, as set out in the judgment of the Supreme Court in *National Thermal Power v. Singer Company And Ors*[3]

FACTUAL BACKGROUND

In brief, Enka, an engineering and construction company, had built a power plant, which was owned by Unipro. The construction contract provided for an arbitration seated in London, governed by the Rules of arbitration of the International Chamber of Commerce. The arbitration clause in the construction contract did not expressly provide the law governing the arbitration agreement and the governing law of the contract.

A fire broke out at the power plant for which Chubb Russia, the insurer, paid US $400 million to Unipro and subrogated the right to claim compensation from third parties. Accordingly, Chubb Russia initiated proceedings before the court in Russia against Enka and other defendants ("**Russian Proceedings**"). During the pendency of the Russian Proceedings, relying on the arbitration agreement, Enka sought an anti-suit injunction before the Commercial Court in England[4] **("English Proceedings")**.

The Commercial Court dismissed Enka's application on the premise that questions regarding the scope of the arbitration agreement and its applicability to the claim in the Russian Proceedings were more appropriately to be determined in the Russian Proceedings. The Commercial Court rejected Enka's argument that the parties' choice of seat was a choice of law for the arbitration agreement but did not determine the law governing the arbitration agreement.[5]

Enka preferred an appeal against the judgment of the Commercial Court before the UK Court of Appeal, who delivered its judgment in April 2020 and granted an anti-suit injunction restraining Chubb Russia from pursuing its claim in the Russian Proceedings.[6] The UK Court of Appeal also held that in absence of an express choice of law governing the arbitration agreement, the law of the seat (here, English law) would apply to the arbitration agreement, as a matter of implied choice.[7] The UK Court of Appeal held that while the express choice of the law applicable to the main contract may sometimes amount to an express choice of the law applicable to the arbitration agreement,[8] however, this conclusion would follow only in a minority of cases and in all other cases there is a strong presumption that the parties have impliedly chosen the law of the seat of the arbitration to govern the arbitration agreement.[9] Considering that the UK Court of Appeal found that arbitration agreement was governed by English law, it went ahead and granted the injunction against the Russian Proceedings.

An appeal was filed before the UK Supreme Court, and the applicable law to the arbitration agreement became the moot issue in the appeal.

JUDGMENT OF THE UK SUPREME COURT AND ANALYSIS: *Position of Law:*[10]

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- The law applicable to the arbitration agreement will be (a) law chosen by the parties to govern it, or (b) absent such choice, the system of law with which the arbitration agreement is most closely connected.
- Where the law applicable to the arbitration agreement is not specified, the choice of governing law of the main contract will generally apply to an arbitration agreement.
- While arriving at this conclusion, the UK Supreme Court also clarified that the choice of a different country as the seat of the arbitration, on its own, is not sufficient to negate an inference that a choice of law for the main contract extends to the arbitration agreement. The Court thereafter set out some instances where the general rule may not apply: (a) if there are provisions at the law of the seat of arbitration which prescribes that where an arbitration is subject to that law, the arbitration agreement will also be treated as governed by that country's law; (b) if there is a serious risk, that if governed by the same law as the main contract, the arbitration agreement would be ineffective.
- Where there is no express choice of law to govern the main contract, the fact that the arbitration is seated in a particular place will not by itself justify an inference that the main contract (or the arbitration agreement) is intended to be governed by the law of that place.
- Where the choice of law to govern the arbitration agreement has not been prescribed, the arbitration agreement has to be governed by the law which it is most closely connected. Where seat has been chosen, it will generally be the seat, even if it differs from the law applicable to the parties' substantive contractual obligations. If the contract requires the parties to undertake good faith negotiations, mediation or any other procedure before invoking arbitration, this will not generally provide a reason to displace the law of the seat of arbitration as the law applicable to the arbitration agreement by default (in absence of a choice of law to govern it).

Reasoning:

The UK Supreme Court held that a choice of law to govern the main contract applies to an arbitration agreement, even when the choice of law differs from that of the place chosen as the seat of arbitration on the following premise.

a. It will provide certainty certainty as the parties can be generally assured that the governing law of the main contract will generally be an effective choice in relation to all of their contractual rights and obligations and to all of their disputes.
b. It will provide consistency, avoid complexities and uncertainties. The UK Supreme Court observed that this approach will be beneficial in a situation where the arbitration agreement is governed by different system of law from the main body of the contract, provisions which requires negotiations, mediations, expert determination before invoking arbitration, as there will be certainty that the governing law of the contract will govern all the aspects. It noted that when the contractual relationship between the parties becomes subject to two distinct systems of law, problems can arise as to where and how to draw the boundaries between them.[11]
c. The artificiality of the arbitration agreement being a separate agreement is a legal doctrine and cannot be used for a determination of the intent of the parties. Parties entering into a commercial contract cannot be deemed to understand a contract with an ancillary or collateral arbitration agreement separate from the underlying contract. Parties would therefore reasonably expect a choice of law to apply to the whole of that contract.[12]
d. This approach is prevalent in a large number of common law and civil law jurisdictions, such as Singapore, India, Pakistan, Germany and Austria. While in Singapore, the approach is different and in *First Link Investments Corpon Ltd. V. GT Payment Pte Ltd [2014] SGHCR 12* it was held that the law of the seat should generally apply to the arbitration agreement.

The UK Supreme Court discussed the provisions of Swedish Arbitration Act and the Arbitration (Scotland) Act 2010,[13] which provide for mandatory application of the law of the seat to the arbitration agreement.[14] The UK Supreme Court also noted that since there are no similar provision in the UK Arbitration Act 1996, it cannot be concluded that a choice of an English seat of arbitration is an implied choice that the arbitration agreement will be governed by English law.[15] In fact, Section 4 (5) of the UK Arbitration Act specifies that where a foreign law is applicable to an arbitration agreement (whether by choice or by applying the closest connection test), that fact alone is enough to disapply the non-mandatory provisions of the UK Arbitration Act.

The UK Supreme Court clarified the decision of the UK Court of Appeal in *Sulamerica*. In Sulamerica, the claims were between the Brazilian companies arising under two insurance policies and the law of the main contract was Brazilian law, with seat in London. The UK Court of Appeal observed that the choice of Brazilian law to govern the contract was a strong indication that the parties intended that system of law to govern the arbitration agreement. However, on the premise that (a) by choosing London as the seat of arbitration, the parties must have foreseen and intended that the provision of UK Arbitration Act should apply to any arbitration; and (b) under Brazilian law, the arbitration agreement could have been enforced only with the insured's consent, and therefore, there was a serious risk that a choice of Brazilian law would significantly undermine the arbitration agreement. The UK Supreme Court rejected the first reasoning in *Sulamerica* on the basis that if the Brazilian law was applicable, then the non-mandatory provisions of the UK Arbitration Act would be excluded and hence, the seat of arbitration being in London would not have any consequence. The UK Supreme Court affirmed the second reasoning, and therefore, the overall ratio of the judgment stands.

Factual Findings:

The UK Supreme Court determined the law governing the underlying contract by applying the closest connection test. Several factors such as, the performance of the contract was to be undertaken in Russia, the compliance required under the Russian law, the use of Russian language, the payment in Roubles into a Russian bank account led to a conclusion that the contract was most closely connected with Russia.[16] Since there was no choice of law governing the contract, the law governing the arbitration agreement had to be determined by applying the closest connection test, and in that regard, London as the seat of arbitration was considered as a close connection in that determination. Accordingly, English law was determined as the law governing the arbitration agreement, and the UK Supreme Court although adopted a different reasoning but upheld the anti-suit injunction passed by the UK Court of Appeal.

Position of law in India:

The Supreme Court of India in *NTPC v. Singer* had held that: (a) the law governing the arbitration agreement is normally the same as the law governing the main contract; (c) Where, however, there is no express choice of the law

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governing the contract as a whole, or the arbitration agreement as such, a presumption may arise that the law of the country where the arbitration is agreed to be held is the law of the arbitration agreement, but, that is only a rebuttable presumption. This judgment was passed is 1992 and is consistent with the approach of the UK Supreme Court.

Analysis:

The law governing the arbitration agreement is hardly ever expressly mentioned in the arbitration clause. However, it has great significance, especially in the context of determination of anti-suit injunction, arbitrability of the disputes and the validity of the arbitration agreement.

The UK Supreme Court has authored a historic judgment, and although it agreed with the decision of the UK Court of Appeal, but the foundation of the judgment is entirely different. The step wise analysis of the law will provide certainty and guidance as to how the law governing arbitration agreement is to be determined. The decision also reflects the intention of the parties (party autonomy), as it carefully marries the position of law with the intention of the parties.

The ratio of the judgment tells us that drafting of the arbitration clause is extremely significant. The best solution would be to mention three separate schemes of laws in the arbitration agreement i.e., law governing the main contract, law governing the arbitration agreement, and the choice of seat of the arbitration. However, in most cases there is no mention of the law governing the arbitration agreement, and in such scenarios, in addition to governing the substantive rights and obligations of the parties, the law governing the main contract will also govern the interpretation and validity of the arbitration agreement, and therefore, must be chosen after careful consideration.

– Alipak Banerjee & Ashish Kabra
You can direct your queries or comments to the authors

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[1] [2020] UKSC 38.
[2] [2012] EWCA Civ 638.
[3] 1993 AIR 998
[4] Before the High Court of Justice Business and Property Courts of England and Wales Queen's Bench Division.
[5] [2019] EWHC 3568 (Comm).
[6] [2020] EWCA Civ 574.
[7] Paragraph 91, Judgment of the UK Court of Appeal.
[8] Paragraph 90, Judgment of the UK Court of Appeal.
[9] Paragraph 91, Judgment of the UK Court of Appeal.
[10] Paragraph 170, Judgment of the UK Supreme Court
[11] Paragraph 53, Judgment of the UK Supreme Court
[12] Paragraph 53(iv), Judgment of the UK Supreme Court
[13] Section 6 of the Arbitration (Scotland) Act, 2010.
[14] Carpatsky Petroleum Corpn v PJSC Ukrnafta [2020] EWHC 769 (Comm); [2020] Bus LR 1284
[15] Paragraph 73 – 76, Judgment of the UK Supreme Court
[16] Paragraph 161, Judgment of the UK Supreme Court