International Arbitration Alert

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The Law of an Arbitration Agreement: Is it the Law of the Seat or the Law of the Underlying Contract? – Paris Contradicts London

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If there is no express law of the arbitration agreement, the law with which that agreement has its closest and most real connection is either the law of the underlying contract or the law of the seat of the arbitration. In *Kabab-Ji SAL v. Kout Food Group*, the English Court of Appeal on January 20, 2020, decided that the law of the underlying contract, English law, governed the arbitration agreement. In contrast, all three arbitrators had already decided that the law of the seat, French law, applied to the issue of validity of the arbitration agreement. Now, the Court of Appeal of Paris ("*Cour d'appel de Paris*"), on June 23, 2020, decided that French law applies to the arbitration agreement by virtue of French law being the law of the seat and pursuant to a substantive rule of international arbitration law that the arbitration clause is legally independent from the underlying contract in which it is included. The *Cour d'appel de Paris*[1] did not find anything in the underlying contract to disturb or derogate from the substantive rules of international arbitration applicable at the seat. On the contrary, it found further comfort in the fact that the underlying contract stated that "[t]he arbitrator(s) shall also apply principles of law generally recognised in international transactions."

- The English Court of Appeal refused enforcement and recognition of the arbitration award.
- The *Cour d'appel de Paris* dismissed the action for annulment of the arbitration award.
- The award **could** be enforced in Paris but not in London. The case raises issues of wider importance to international commercial arbitration.

Our International Arbitration Alert of January 30, 2020, looked at the facts and the London Court of Appeal's jurisprudence. In this Alert, we focus on the approach adopted by the *Cour d'appel de Paris* in its ruling dated June 23, 2020. The differing desire in the two courts in respect of the primacy of the substantive rule of international arbitration law that an arbitration agreement is legally independent from the underlying contract is tangible.

The Approach in the *Cour d'appel de Paris*

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French courts ordinarily seek to give maximum legal effect to agreements to arbitrate. French courts have held that international arbitration agreements are "autonomous" from any national legal system and, as a consequence, are directly subject to general principles of international law. For example, the French Supreme Court's ("*Cour de cassation's*") landmark *Dalico*[2] decision held:

according to a substantive rule of international arbitration law, the arbitration cause is legally independent from the main contract in which it is included or which refers to it and, provided that no mandatory provision of French law or international public policy (ordre public) is affected, that its existence and its validity depends only on the common intention of the parties, without it being necessary to make reference to a national law.

In other words, the French *Cour de cassation* chose not to apply a conflict-of-laws analysis when considering the validity of an arbitration agreement, but to turn to the relevant facts and examine the common intent of the parties, i.e., to apply the French substantive rules of international arbitration to the arbitration agreement. There was a possibility, however, that the *Unikod*[3] decision (which announced a slight evolution of French law because it appeared to reserve the application of a law specifically chosen by the parties to govern the arbitration agreement, and thus seemed to reintroduce, in part, the conflict-of-laws analysis) could prevail. It did not prevail.

The *Cour d'appel de Paris* found that the fundamental starting point was the substantive rule of international arbitration law, meaning that the arbitration agreement is legally independent from the underlying contract in which it is included and its existence and validity are interpreted subject to the law of the seat unless there is a clear objective common will of the parties to have a different approach. The *Cour d'appel de Paris* did not find that the parties had derogated from the substantive rule (as the English Court of Appeal had concluded in January 2020). The *Cour d'appel de Paris* stated the following:

The designation of English Law as generally governing the Agreements and the prohibition on arbitrators not to apply a rule which would contradict the Agreements are not in themselves sufficient to establish the common will of the parties to submit the arbitration clauses to English law and thus to derogate from the substantive rules of international arbitration applicable at the seat of arbitration expressly designated by the parties.

On the contrary, the Agreements provide at Article 14.3 of the FDA and 26.3 of the FOAs that "The Arbitrator(s) shall also apply principles of law generally recognised in international transactions."

Further, contrary to *Kout Food Group's* assertion, no express provision was actually agreed between the parties that would designate English law as governing the arbitration clause, and so, applying the substantive law of the seat, in accordance with generally recognized principles of law, the arbitral tribunal did not apply a rule that would contradict the wording of the agreements. Likewise, *Kout Food Group* did not provide evidence of circumstances such as to establish unequivocally the common will of the parties to designate English law as governing the validity, transfer or extension of the arbitration clause. In response to *Kout Food Group*'s claim, according to which it did not have the capacity to sign an arbitration agreement under the Kuwaiti Civil Code, the *Cour d'appel de Paris* asserted that the doctrine of separability of the

arbitration clause is of general application, as an international substantive rule sanctioning the lawfulness of the arbitration clause, without any reference to a system of conflict of laws, the validity of the agreement having to be reviewed solely in the light of the requirements of international public policy, irrespective of any national law, even that governing the form or substance of the contract containing it. In consequence, the provisions of the Kuwaiti Civil Code, that do not form part of either the mandatory rules of French law or international public policy are inapplicable for the purpose of assessing the existence or effectiveness of the arbitration clause. The award[4] would not be annulled.

The Clash Between London and Paris Confirmed

The inconsistency of the two judgements is also heightened by the fact that, as explained in our International Arbitration Alert, French case law tends to suggest that an arbitration agreement could extend to all companies in a group, including those that are not signatories. This approach was indeed confirmed by the *Cour d'appel de Paris* when it considered that having regard to the organizational chart of *Kout Food Group* and its participation in the performance of the contract, it was "more than sufficient" under French law to make it a party to the arbitration clause.

The confrontation between the two countries' courts could have been avoided if the English Court of Appeal had decided to stay the proceedings to await a decision of the court of the seat[5]; yet it had declared that a stay was not necessary[6]. Now it appears that the sequence in which the enforcement judge and the annulment judge render their decisions proves to be more important than one might have thought.

[1] Paris, pôle 1 - ch. 1, 23 Juin 2020 (n° 17/22943).

[2] Judgement of 20 December 1993, *Municipalité de Khoms El Mergeb v. Société Dalico (Cour de cassation chambre civile).*

[3] Judgement of 30 March 2004, *Société Unikod contre Société Ouralkali (Cour de cassation, première chambre civile*). Yet, in the *Unikod* decision, the Court, referring to the principle of separability, in fact disregarded the choice of a state law to govern the main contract as an indication of the parties' choice as to the law applicable to the Arbitration Agreement.

[4] The award rendered in Paris on September 11, 2017, ruled by a majority that Kabab-Ji was entitled to all unpaid monthly license fees between 2008 and 2011 in the sum of USD 892,945, to USD 4,631,841 as compensation for Kabab-Ji's loss of chance claim, to USD 1,490,645.19 as Kabab-Ji's reasonable costs of Arbitration, and to interest at 7% per annum on all sums awarded from the date of the award.

[5] This is one of the arguments of Kabab-Ji's appeal yet to be heard before the UK Supreme Court.

[6] Kabab-Ji SAL v Kout Food Group [2020] EWCA Civ 6 at [81]