International Arbitration Alert

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Enka v Chubb: The Nuanced Presumptions 'test' on the Law of Arbitration Agreements

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The United Kingdom Supreme Court in *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb*[1]has now resolved the question: which system of national law governs the validity and scope of an arbitration agreement when the law applicable to the contract containing it differs from the law of the seat of the arbitration? Will it be the law governing the contract; the law governing the procedure (the law of the seat); or another system of national law altogether? Noting that this issue "*has long divided courts and commentators, both in this country and internationally*"[2] the Supreme Court has provided an elegant and nuanced answer which in practice will require application of rules of contractual interpretation of English law. Put simply:

- where the law applicable to the arbitration agreement is not specified, a choice of governing law for the contract will **generally** apply to an arbitration agreement which forms part of the contract.
- In the absence of any choice of law to govern the contract, the arbitration agreement is governed by the law with which it is most closely connected. Where the parties have chosen a seat of arbitration, this will as a rule of law **generally** be the law of the seat, even if this differs from the law applicable to the parties' substantive contractual obligations.
- The fact that the contract requires the parties to attempt to resolve a dispute through good faith negotiation, mediation or any other procedure before referring it to arbitration 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 the absence of a choice of law to govern it.

Enka addresses an important issue in international arbitration. For example, the interpretation and validity of the arbitration agreement can be a fundamental issue at the start of a dispute and especially so when there are questions about the coverage of the arbitration agreement to other parties. An obvious but perhaps unavoidable consequence of the layered presumptions in *Enka* is a potential dichotomy between the 'governing law' answer in England as opposed to an answer favoring the seat at the law of the country where the award was made. We say this because Article V(1(a) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards provides that the validity of the arbitration agreement should be verified, "failing any indication [of

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the law of the arbitration agreement by the Parties], under the law of the country where the award was made".

The Facts

The claimant, a Turkish construction company, was a sub-contractor providing certain building works on the construction of a power plant in Russia. In the construction contract there was an arbitration agreement providing for arbitration under the ICC Rules with the Seat in England.[3]The contract did not expressly state what law governed the contract or what law governed the arbitration agreement. The contract, however, provided Russian law governed specified provisions in it. Following a fire on the power plant, the insurers (including the first defendant) paid approximately USD 400 million to the owner under an insurance policy, resulting in them becoming subrogated to the owner's rights against the claimant (which had been assigned by the main contractor to the owner). The first defendant commenced a claim against the claimant (and a number of other defendants) in the Russian Court in May 2019 for damage arising out of the fire. The claimant issued a claim in the English Court seeking an anti-suit injunction restraining the claim before the Russian Court on the basis that it breached the arbitration agreement.

The 'new' approach to derive law of an Arbitration Agreement

The Supreme Court noted that the issue of determining the law applicable to the arbitration agreement has long divided courts and commentators, both in England and internationally:

"On one side 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. On the other side there are those who say that the law of the chosen seat of the arbitration should also generally govern the arbitration agreement. There have been Court of Appeal decisions falling on either side of this divide: Sulamérica Cia Nacional de Seguros SA v Enesa Engenharia SA [2013] 1 WLR 102 and C v D [2008] Bus LR 843".[4]

The Supreme Court decided that, as a starting point, the arbitration agreement is governed by: (i) the law expressly or impliedly chosen by the parties to govern it (applying the rules of contractual interpretation of the law of the forum); or (ii) in the absence of such a choice, the law "with which it is most closely connected". This common-law position is not controversial. However, the Court also laid down the following "concluding" principles at Paragraph 170 of the Judgment:

A) If parties have chosen (expressly or impliedly) a governing law of the contract

- The governing law of the contract will generally apply to the arbitration agreement. The Supreme Court stipulated that there were "strong reasons" as a matter of principle and authority that an agreement on a law to govern a contract should generally be construed as applying to an arbitration agreement in that contract. The majority of English case law proceeded on this assumption, most recently the Court of Appeal decision in *Kabab-Ji SAL (Lebanon) v Kout Food Group (Kuwait)* [2020] 1 Lloyd's Rep 269. This approach is said to promote certainty and consistency.
- The choice of a different country as the seat of the arbitration does not in itself displace this presumption. However, the law of the seat may trump the governing law if provision(s) of the law of the seat indicate that, where an arbitration is subject

to that law, the arbitration agreement will also be treated as governed by that country's law; or there is a serious risk that the arbitration agreement would be ineffective if the governing law is used.

B) If parties have not chosen a governing law of the Contract

- The election of a seat of arbitration will not by itself justify an inference that the law of the seat governs the arbitration agreement; the Court must apply the "most closely connection test".
- However, in practice, the arbitration agreement will generally be most closely connected to and thus governed by the law of the seat.

The death of Severability?

Whilst the Court of Appeal and the Supreme Court reached the same outcome (that English law governed the Arbitration Agreement), the Supreme Court rejected the reasoning of the Court of Appeal. The Court of Appeal had advocated a "strong presumption" that, by nominating a seat of the arbitration, the parties had impliedly chosen that the law of that seat should govern the arbitration agreement in the absence of "powerful countervailing factors". The Supreme Court found that the Court of Appeal had put too much emphasis on the separability doctrine. The purpose of this doctrine was "not to insulate the arbitration agreement from the substantive contract for all purposes" but merely to give legal effect to the parties' presumed intention that their agreed procedure for resolving disputes should remain effective in circumstances that would render the substantive contract ineffective.[5]

To further support their approach, at least when there is an express choice of governing law for the contract, the Supreme Court suggests that such approach is generally followed at an international level.[6] However, the Supreme Court acknowledged that "there is no uniformity" and, as suggested by Professor Dr. Maxi Scherer in the Akin Gump Arbitration Lecture 2020, there is no prevailing "solution" worldwide. For example, the French Courts approach the issue differently, and French judges have held that arbitration agreements are "autonomous" from any national legal system and, as a consequence, are directly subject to general principles of international law.[7] The clash between the French and English approaches has been at the center of the ***Kabab-Ji v. Kout Food*** saga.[8] In *Enka* the Supreme Court disregarded the "separability doctrine" preferring to favor a commercial practice point of view:

"The principle that an arbitration agreement is separable from the contract containing it is an important part of arbitration law but it is a legal doctrine and one which is likely to be much better known to arbitration lawyers than to commercial parties. For them a contract is a contract; not a contract with an ancillary or collateral or interior arbitration agreement. They would therefore reasonably expect a choice of law to apply to the whole of that contract."[9]

In Switzerland, the approach is also different as the Swiss Private International Law on Arbitration (PILA) codifies the "validation principle" which is recalled by the Supreme Court judges as to be a well-established principle according to which "an interpretation which upholds the validity of a transaction is to be preferred to one which would render it invalid or ineffective".[10] Article 178(2) PILA specifically provides: "an arbitration agreement is valid if it conforms either to the law chosen by the parties, or to the law governing the subject-matter of the dispute, in particular the main contract, or to Swiss law."

Practical application of the nuanced rules

The presumptions proposed by the Supreme Court in *Enka* in practice will be complex. For instance, if a contract provides that the governing law is Swiss law and the arbitration agreement specifies a seat in Sweden, the presumptive conclusion should be that Swiss law will govern the arbitration agreement. However, one would need to check that Swiss

law does not invalidate the arbitration agreement; and check if Swedish law dictates that the law of the Seat should govern the arbitration agreement. Further, this exercise can create risk of inconsistency between national Courts such as in the *Dallah*,[11] *Kabab-Ji*[12] and (most probably) *PT Ventures*[13] where judges need to evaluate French law, however, the French judges did not reach the same decision.

Some arbitration centers suggest that contracts should incorporate a specific choice of law for the arbitration agreement by virtue of the arbitral rules selected in the arbitration agreement. For example, the 202 LCIA Arbitration Rules at Article 16.4 provides:

"[…] the law applicable to the Arbitration Agreement and the arbitration shall be the **law applicable at the seat of the arbitration**, unless and to the extent that the parties have agreed in writing on the application of other laws or rules of law and such agreement is not prohibited by the law applicable at the arbitral seat." (emphasis added)

It remains to be seen whether this is the last word on the issue; the fact that the Supreme Court Justices were divided three to two in its judgment[14] could indicate that this debate is set to continue. In this context, permission to appeal the Court of Appeal case of *Kabab-Ji* was granted on 8 July 2020.

1 *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb* [2020] UKSC 38; [2020] 1 WLR 4117 9 ("*Enka*")

2 *Enka* para. 3.

3 An assignment agreement was subsequently executed which assigned all rights of the main contractor against the claimant to the owner and provided that all disputes between the owner and the claimant should be resolved in accordance with the arbitration agreement.

4 *Enka* para. 3.

5 *Enka* paras 60 to 64.

6 *Enka* paras 55 to 58.

7 Landmark decision of the French *Cour de cassation* in its Judgement of 30 March 2004, Société Unikod contre Société Ouralkali (Cour de cassation, première chambre civile).

8 *Kabab-Ji SAL v Kout Food Group* [2020] EWCA Civ 6 at [81] and Cour d'appel de Paris, pôle 1 - ch. 1, 23 Juin 2020 (n° 17/22943).

9 *Enka* para 53(iv).

10 *Enka* para. 95.

11 *Dallah Real Estate and Tourism Holding Company v The Ministry of Religious Affairs, Government of Pakistan* [2010] 3 W.L.R. 1472 (3 November 2010) and Gouvernement du Pakistan – Ministère des Affaires

Religieuses v. Dallah Real Estate and Tourism Holding Company (Case No. 09/28533)

12 *Kabab-Ji SAL v Kout Food Group* [2020] EWCA Civ 6 at [81] and Cour d'appel de Paris, pôle 1 - ch. 1, 23 Juin 2020 (n° 17/22943). See also Akin Gump International Alerts on the cases.

13 *PT Ventures SGPS SA v Vidatel* Ltd (BVIHC (COM) 2015/0017 and 2019/0067, 13 August 2020.) See also Akin Gump International Alerts on the case.

14 Two of the Supreme Court Justices (Lord Burrows and Lord Sales) gave a powerful dissenting opinion, stressing that it was desirable to have the same law governing the main contract and the arbitration agreement and thus opining that it was unhelpful to impose a general rule that in the absence of a choice of law for the main contract, an arbitration agreement will have its closest and most real connection with the law of the Seat. In contrast, there should be a general presumption that an arbitration agreement is in fact most closely connected with the law of the main contract.