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Choice of Law for Arbitration Agreements: A Case Comment on Enka Insaat Ve Sanayi AS v. OOO Insurance Company Chubb, [2020] UKSC 38

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A recent decision of the U.K. Supreme Court may help clarify which law governs an arbitration clause in a commercial contract when the parties have not made that preference explicit.

An international commercial contract containing an arbitration clause potentially engages three separate systems of law. The first is the law of the main contract containing the arbitration clause. The second is the procedural law of the arbitration, which is the arbitration law of the "seat" or the place chosen for the arbitration in the arbitration clause. The third system that may be relevant is the law of the arbitration clause, which governs, among other things, the validity and scope of the parties' agreement to submit disputes to arbitration.

Parties to international commercial contracts often include an express choice of law for both the main contract and the seat of the arbitration, but do not typically do so for the law that governs the arbitration clause itself. For example, the parties may stipulate that their agreement is governed by Russian law, with any disputes to be resolved through arbitration in London, England. In this instance, the law of the main contract is the law of Russia and the procedural law of the arbitration is that of England. But what law governs questions about the arbitration clause itself?

The law applicable to the arbitration clause is a significant issue to consider when drafting international contracts that provide for arbitration. In particular, where the parties choose the law of one jurisdiction to govern the main contract and provide for the seat of arbitration in a different jurisdiction, important issues such as whether a dispute falls within the scope of the arbitration clause or whether the clause is invalid, may be decided differently under these different legal systems. This scenario gives rise to the difficult question of whether the parties intended the arbitration clause to be governed by the law of the main contract or by the law of the seat.v

The U.K. Supreme Court has recently provided helpful guidance on this question in Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb, [2020] UKSC 38. It established a general rule that a choice of law for the main contract should be construed as the parties' implied choice of law for their agreement to arbitrate, even where the main contract law differs from the seat of the arbitration. In the absence of any choice of law, however, the Court found that the law of the seat of the arbitration will generally be the most closely connected legal system to the agreement to arbitrate and, thus, the applicable law for the

arbitration clause.

Background facts and procedural history

In February 2016, a power plant in Berezovskaya, Russia, was severely damaged by fire. Enka was a subcontractor involved in the construction of the plant. Chubb was the insurer for the owner of the plant. The owner had taken an assignment of the rights that the general contractor held under its subcontract with Enka. In May 2019, exercising its right of subrogation, Chubb commenced proceedings in a Moscow court against Enka for damages in relation to the fire at the plant.

Enka's subcontract, however, included a term providing for arbitration pursuant to the International Chamber of Commerce's arbitration rules, with London, England as the place of the arbitration. Enka commenced proceedings in the Commercial Court in England, seeking an order restraining Chubb from litigating in violation of the arbitration clause (anti-suit injunction). It also applied to the Moscow court for a stay of the litigation.

The parties took opposing positions on the law applicable to the arbitration clause. Chubb argued that the arbitration clause was governed by Russian law because the parties impliedly chose Russian law for the main contract. It also argued that the English Commercial Court should decline to rule on the issue as a matter of judicial comity[1] or discretion given the stay proceedings pending in the Moscow court. Enka, on the other hand, argued that the arbitration clause was governed by English law as the law of the seat. It also took the position that an English court could grant an anti-suit injunction regardless of the applicable law because the arbitration was seated in England.

The Commercial Court dismissed Enka's claim for an anti-suit injunction on the grounds that England was not the most appropriate forum to seek such relief[2]. The English Court of Appeal reversed the Commercial Court's decision and granted the anti-suit injunction. The Court of Appeal found that the seat of the arbitration is always an appropriate forum in which to seek an anti-suit injunction[3]. The Court of Appeal also established a general rule that in the absence of an express choice of law for the arbitration agreement, the law of the seat should be considered the parties' presumptive implied choice of law for the arbitration clause[4].

The supreme court's decision

A 3–2 majority of the U.K. Supreme Court dismissed Chubb's appeal, thereby affirming the English Court of Appeal's decision to grant an anti-suit injunction. All five members of the panel, however, disagreed with the Court of Appeal's ruling that the law of the seat should be the presumptive choice of law for the arbitration clause. Instead, they found that when the parties' had chosen a law to govern the main contract, that choice should be their presumptive choice for the arbitration clause.

Lord Hamblen and Lord Leggat wrote for the majority (the "Majority"). They began with the familiar two step choice of law analysis from the common law which provides that a contract is governed by: (1) the law expressly or impliedly chosen by the parties or (2), in the absence of such a choice, the law with which the contract has its closest and most real connection[5]. Applying this framework, the Majority found that a choice of law for the main contract, whether express or implied, should generally be construed as an implied choice of law for the arbitration clause[6]. The dissenting justices, Lord Burrows and Lord Sales (the "Dissent"),

agreed with the Majority on this point[7]. The Majority relied on the simple logic that "the arbitration clause is part of the contract which the parties have agreed is to be governed by the specified system of law[8]." They reasoned that this approach would provide certainty, consistency, and coherence, while avoiding needless complexity and artificiality[9]. It is, noteworthy, however, that this is only a presumption of implied choice which may be rebutted where the circumstances warrant a different inference.

The Majority also provided guidance on when the presumption may be rebutted. In particular, the Majority reaffirmed what they styled the "validation principle," a general principle of contractual interpretation that provides that an interpretation that upholds the validity of the contract is to be preferred to one that would render it invalid or commercially ineffective[10]. In the Majority's view, if there is a serious risk that the arbitration clause would be invalid or ineffective under the law chosen for the main contract, this grounds an inference that the parties likely did not intend for their arbitration clause to be governed by that law. In addition, the Majority acknowledged that a choice of seat may entail an implied choice of law for the arbitration agreement where the law of the seat requires that an arbitration subject to its procedural law must also be subject to its substantive law concerning arbitration clauses[11].

In the absence of an express or implied choice of law for the main contract or for the arbitration clause, the Majority found that the law of the seat generally has the closest and most real connection to the arbitration clause[12]. This is so because the common law places great weight on the place of performance as a connecting factor, and the seat is the place of performance of the arbitration agreement[13]. The law of the main contract, by contrast, is less likely to have as significant a connection to the arbitration clause, because the substantive obligations in the main contract address a different subject matter and purpose than the arbitration agreement, and parties often purposefully choose a neutral seat with no connection to the place of performance of the substantive obligations in the main contract[14]. The Majority also pointed out that their approach was consistent with article 36(1)(a)(i) of the UNCITRAL Model Law and article V(1)(a)of the New York Convention, which have been interpreted to suggest that the law of the seat should be considered a strong connecting factor in the choice of law analysis[15].The Dissent parted ways with the Majority on this point, because, in their view, the law of the main contract generally has the closer and more real connection to the arbitration clause[16].

The Majority also commented on the Commercial Court's comment that England might not be the most appropriate forum to grant an anti-suit injunction. In the Majority's view, this was an error, as the effect of choosing London, England, as the seat is a submission to the jurisdiction of the English courts to grant injunctive relief to restrain parties that are found to be in breach of their agreement to arbitrate[17]. In response to Chubbs's argument that an English court should nonetheless defer to the foreign court as a matter of comity, the Majority stated that comity had "little if any role to play where anti-suit injunctive relief is sought on the grounds of breach of contract[18]." The Dissent agreed with the Majority that the English courts were not required to defer their decision pending the outcome of proceedings in a foreign court[19].

Turning to the merits of the appeal, the Majority found that the subcontract did not contain either an express or implied choice of law[20]. They therefore concluded that the law of the arbitration agreement was English law, because the seat of the arbitration was London, England[21]. Chubb did not dispute that if the arbitration clause were to be governed by

English law, then there would be no basis to interfere with the Court of Appeal's order. On this basis, the Majority dismissed the appeal. The Dissent, however, would have found that the parties impliedly chose Russian law to govern the subcontract and this choice extended to the arbitration clause[22]. As a result, the Dissent would have remitted the claim back to the Commercial Court to decide the issues under Russian law.

Comment

The U.K. Supreme Court's decision provides welcome guidance on a common law issue that is underdeveloped in the Canadian jurisprudence. It is worth noting that the foundational pillars of the Majority's reasoning are generally applicable throughout Canada's common law jurisdictions. Canadian common law jurisprudence employs the same two step choice of law framework for contracts[23]. The common law provinces have enacted legislation implementing the UNCITRAL Model Law and the New York Convention, which, as mentioned above, include provisions suggesting that the law of the seat should be a strong connecting factor in the absence of a choice of law. Thus, the U.K. Supreme Court's decision appears poised to serve as strong persuasive authority for a court or arbitral tribunal applying Canadian common law choice of law rules to international contracts which contain an agreement to arbitrate.

The situation in respect of interprovincial contracts is, however, not as clear. Common law choice of law rules also apply to interprovincial contracts[24]. But, there is no equivalent to article 36(1)(a)(i) of the UNCITRAL Model Law and article V(1)(a) of the New York Convention in domestic arbitration legislation to suggest a default rule in favour of the law of the seat in the absence of a choice of law. Therefore, the Dissent's approach of favouring the main contract law over the law of the seat as having a closer and more real connection to the arbitration clause could carry some weight in the case of domestic arbitrations providing for a place of arbitration that differs from the main contract law. Nonetheless, Canadian jurisprudence reflects cohesive choice of law rules, as opposed to differentiating between international contracts and interprovincial contracts.

Overall, the U.K. Supreme Court's decision to establish a general rule favouring the parties' choice of law for the main contract as an implied choice of law for the arbitration clause appears to accord with commercial practice and commercial expectations. It is not uncommon to see governing law clauses and arbitration clauses drafted alongside one another in international contracts. Nonetheless, parties that prioritize certainty in terms of the applicable law governing their arbitration agreement may consider expressing a specific choice of law for the arbitration clause in their contract. Parties should remain cognizant, however, that an express choice of law for the arbitration agreement leaves little, if any, room for the operation of the principle of validation if the choice of law would result in an unenforceable arbitration clause. As always, great care should be taken in choosing the seat, the main contract law, and law of the arbitration clause, given their significance to ensuring the effectiveness of the parties' commitment to submit disputes to arbitration.

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[1] The phrase “judicial comity” refers to the deference and respect which domestic courts accord to the decisions of foreign courts. [2] Enka Insaat Ve Sanayi AS v OOO “Insurance Company Chubb” & Ors, [2019] EWHC 3568 (Comm), at para 113. [3] Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb & Ors, [2020] EWCA Civ 574, at para 42. [4] Ibid, at paras 91, 109. [5] Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb, [2020] UKSC 38, at para 27. Some courts break the test into three components: (1) express choice of law; (2) implied choice of law; and (3) most real and substantial connection. There does not, however, appear to be any substantive difference between these different formulations. See BNA v. BNB, [2019] SGCA 84, at paras 44-48. [6] Ibid, at para 170(iv). [7] Ibid, at para 266. [8] Ibid, at paras 43-58. [9] Ibid, at para 53. [10] Ibid, at paras 95-109. [11] Ibid, at para 94. [12] Ibid, at para 121. [13] Ibid, at para 121. [14] Ibid, at paras 122-123. [15] Ibid, at paras 127-128, 132-136. [16] Ibid, at para 257. [17] Ibid, at paras 174, 179. [18] Ibid, at para 180. [19] Ibid, at paras 261, 293. [20] Ibid, at para 155. [21] Ibid, at paras 156-169, 171. [22] Ibid, at paras 207-230. [23] Imperial Life Assurance Co. of Canada v. Segundo Casteleiro Y Colmenares,[1967] SCR 44, 62 DLR (2d) 138; Vita Food Products Inc. v. Unus Shipping Company, [1939] AC 277, [1939] 1 All ER 513 (JCPC). [24] Lilydale Cooperative Limited v. Meyn Canada Inc., 2015 ONCA 281.