Laying down the law

Establishing the proper law of an arbitration agreement is key, says **Khawar Qureshi QC**

IN BRIEF

- It should not be assumed that the proper law of a contract will also apply to its arbitration clause.
- The law of the seat may be applied as the proper law of an arbitration clause in certain circumstances.
- Parties should expressly identify the proper law of the arbitration agreement to avoid doubt.

In the case of *Sulamérica Cia Nacional De Seguros SA v Enesa Engenharia SA* [2012] EWCA Civ 638, [2012] All ER (D) 145 (May), the Court of Appeal underlined the significance of the choice of the seat of arbitration (London in that case). This could give rise to unexpected consequences, where parties have hitherto assumed that the choice of governing law for the agreement also meant that the same law applied to the arbitration agreement.

The decision is not without controversy, and may be criticised by some as being an example of an unduly "pro-London arbitration" approach on the part of the English courts, which may also generate uncertainty in international contracts containing London arbitration clauses. However, the decision makes it all the more important to ensure that the dispute resolution clause in a contract is drafted carefully, and expressly identifies the law applicable to the arbitration agreement.

The facts

The case concerned claims under two similar policies of insurance ("the policy") relating to the construction of a Hydro-electric power plant in Brazil. The insured claimed under the policy in March 2011, but the insurers declined liability on the basis that the losses were excluded or uninsured.

The parties, the subject matter of the insurance and the currency of the policy were all Brazilian. The policy was written in Portuguese and English.

The policy contained two potentially conflicting clauses; a London (ARIAS) arbitration clause, and an exclusive jurisdiction clause in favour of the courts of Brazil. The parties had expressly chosen Brazilian law as the law governing the contract. Under Brazilian law, it appeared to be common ground that an arbitration clause can only be invoked with the consent of the other party. This particular feature of Brazilian law appears to have played an important part in the reasoning of the Court of Appeal.

The insurers gave notice of arbitration. In response, the insured sought to establish that the insurers were not entitled to refer the dispute to arbitration and obtained an injunction from the court in São Paulo restraining the insurers from resorting to arbitration. The insurers then made an application without notice to the commercial court, seeking an injunction to restrain the insured from pursuing the proceedings in Brazil. This was granted by Cooke J.

The Court of Appeal was faced with the question of whether to continue the injunction, which required analysis of the arbitration agreement and its effect. If the insured's position was upheld (and Brazilian Law applied to the arbitration agreement), the reference to arbitration would be ineffective and the injunction would have to be discharged.

The issues

The insured advanced four arguments to support their submission that Brazilian law was the law of choice for the arbitration agreement:

(i) the express choice of the law of Brazil as the law governing the policy;
(ii) the agreement that the courts of Brazil should have exclusive jurisdiction in respect of any disputes in connection with the policy;
(iii) the close commercial connection between the policy and the state of Brazil; and
(iv) the inclusion of a mediation provision, governed by the law of Brazil, requiring the parties to attempt mediation as a pre-condition to any reference to arbitration.

The insurers relied on the doctrine of separability (as reflected in s 7 of the Arbitration Act 1996) (AA 1996) to contend that the arbitration agreement should be governed by the law of the seat, namely English law. The insurers also pointed to the "steer" provided by the House of Lords in the case of *Fiona Trust v. Privalov* [2007] UKHL 40, [2007] 4 All ER 951, in favour of interpreting an arbitration agreement so as to give effect to the choice of "one stop" dispute resolution by arbitration.

The Court of Appeal's reasoning

The main judgment was given by Moore-Bick LJ (with Lord Neuberger MR providing a separate short supporting judgment). Their lordships' emphasised the importance of the doctrine of separability, which operates to insulate arbitration agreements from invalidating defects in the main contract.

In finding that English law applied to the arbitration agreement, Moore-Bick LJ considered previous case law in which observations had been made as to the proper law of the arbitration agreement. Nevertheless, it would appear that the Court of Appeal adopted a "post *Fiona-Trust* approach", and applied the obiter dicta by Longmore LJ in *C v D* [2007] EWCA Civ 1282, [2008] 1 All ER (Comm) 1001 where it was observed that "it would be rare for the law of the arbitration agreement to be different from the law of the seat of the arbitration".

In terms of the critical factors in the decision, it would appear that the reasoning of the Court of Appeal placed heavy emphasis upon the consequences of choosing London as the seat of any arbitration, thus engaging the AA 1996. Indeed, Moore-Bick LJ observed as follows: "As the parties must have been aware, the choice of another country as the seat of the arbitration inevitably imports an acceptance that the law of that country relating to the conduct and supervision of arbitrations will apply to the proceedings…The parties must have forseen and intended that [the AA 1996] would apply including all those provisions such as ss 5, 7, 8, 12, and 13 which are more substantive than procedural. This tends to suggest that the parties intended English law to govern all aspects of the arbitration agreement."

Equally powerful was the apparent effect of Brazilian law which would render the arbitration agreement unenforceable without the consent to arbitrate of the insured. This appeared to be the main reason why the court "was unable to accept" that the parties had made an implied choice of Brazilian law to govern the arbitration agreement. The Master of the Rolls considered this to be a "pretty strong argument for English Law applying".

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Concluding observations.

There will be some commentators who view the Court of Appeal's decision as choosing between two equal fictions—namely, that the parties must be taken to understand the full consequence and effect of the choice of London as the seat of an arbitration, and must also be taken to have impliedly excluded Brazilian law as the proper law of the arbitration agreement.

However, at its core, the Court of Appeal's decision seeks to ensure that an agreement to arbitrate is upheld, and interpreted as effective where possible. On that reading, the decision is likely to be seen as another strong signal that London is the place to arbitrate. NLJ

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