U.K. Supreme Court Clarifies How to Determine the Governing Law of Arbitration Agreements

October 30, 2020

In a landmark decision set to become the leading authority on the governing law of arbitration agreements, the U.K. Supreme Court recently handed down judgment in *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb* [2020] UKSC 38. The judgment brings some much-needed certainty on how English courts will determine the law applicable to arbitration agreements in future cases.

The Issue Before the Court

The applicable law of an arbitration agreement can have very important practical consequences for the parties, such as whether a non-signatory can be a party to the arbitration, whether pre-contractual negotiations are admissible evidence, whether tort claims are within the scope of the arbitration agreement, and even whether the arbitration agreement is valid at all.

Nevertheless, it is rare for such applicable law to be expressly set out in the parties’ contract. Consequently, English courts – up to the level of the Court of Appeal – had been called upon a number of times to decide which law applied. Regrettably, their reasoning and decisions were far from consistent. In summary, two different approaches had emerged, as follows:

1. The “main contract” approach: presuming that the parties intended the same system of law to govern their arbitration agreement as would govern their main contract.
2. The “seat” approach: presuming that the parties intended their arbitration agreement to be governed by the law of the seat that they chose for the arbitration.

It was therefore hard to predict what approach the English courts might take in a given case. Thankfully, the Supreme Court decision has now provided some real clarity on this issue (despite a 3:2 divide between the Justices), as discussed below.

The Majority Judgment

The majority (Lords Hamblen, Leggatt and Kerr) began by explaining that, because the Rome I Regulation (on the law applicable to contractual obligations) expressly excludes arbitration agreements from its scope, the question must be answered by applying common law rules. Applying those rules, they set out the following approach to determining the law governing arbitration agreements.

1. The law chosen by the parties for their main contract

The court must first ascertain, through ordinary principles of contractual interpretation, whether the parties have chosen a system of law to govern their main contract. If they have made such a choice – whether expressly or impliedly – then this system of law will also apply to their arbitration agreement, unless there exists a “good reason to the contrary.”
The majority gave two examples of what might constitute a good reason to the contrary – namely: (i) there is a real risk that the parties’ arbitration agreement would be invalid according to the law of the main contract; and (ii) there is a provision in the law of the seat indicating that, where the parties have chosen that seat, the arbitration agreement will be governed by that law.

II. The law most closely connected with the arbitration agreement

If the parties have not chosen a system of law to govern their main contract, their arbitration agreement will be governed by “the law with which the arbitration agreement is most closely connected.” This will, as a general rule, be the law of the seat of the arbitration. Ultimately, therefore, the majority favoured the “seat” approach.

The Dissenting Judgments

Lords Burrows and Sales each gave dissenting judgments. They agreed with the majority that, where the parties have (expressly or impliedly) chosen the governing law for their main contract, that law should also apply to their arbitration agreement. But, where the parties have made no such choice, they preferred the “main contract” approach: the court should determine the governing law of the main contract under Rome I, and presume that the parties intended the same law to govern their arbitration agreement.

Practical Tips

As was the case before this judgment, the best approach is for parties to consider the law that they wish to apply to their arbitration agreement, and clearly state their choice in the arbitration clause of their contract, for example as follows: “This arbitration agreement is to be governed by and construed by the laws of [country].” This should provide them with certainty as to which law will govern their arbitration.

If this is not possible (and indeed in any event), parties should clearly express the system of law that they have chosen to govern their main contract, with the knowledge that – following this judgment – this law will also apply to their arbitration agreement, other than in exceptional circumstances.

If the parties make no express choice of law for either their main contract or arbitration agreement, there may be uncertainty as to which law will apply to the latter, depending on whether or not the court can imply a choice of law for the main contract. If it can, then this law will likely govern the arbitration agreement; but if it cannot, the law of the seat of the arbitration is likely to apply. Given the scope for different opinions on when an implied choice of law has been made (as is evident from the divergent views of the majority and minority in this case), this is a situation that parties should seek to avoid.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Nicola Phillips
Partner – London
Phone: +44.20.7413.1317
Email: nphillips@crowell.com

Robert Weekes
Partner – London
Phone: +44.20.7413.1320
Email: rweekes@crowell.com

Laurence Winston
Partner – London
Phone: +44.20.7413.1333
Email: lwinston@crowell.com

David Russell, CFA
Associate (Barrister) – London
Phone: +44.20.7413.1358
Email: drussell@crowell.com