Main Contract Approach vs Seat Approach – How to Determine the Proper Law of the Arbitration Agreement?

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Introduction

The determination of the proper law of the arbitration agreement has been subject to some debate recently. Previous judgments have oscillated between the "main contract" approach (which says that the substantive law of the contract should be the proper law) and the "seat" approach (which says that the proper law should be the law of the seat of arbitration).

In *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb* [2020] UKSC 38 ("**Enka v Chubb**'), the Supreme Court of the UK held in favour of the "main contract" approach. We discuss the judgment of the UK Supreme Court, as well as the implications going forwards.

Starting Point – Proper Law vs Other Laws/Rules

Before we begin, it is important to understand the proper law of the arbitration agreement (which determines the validity and scope of an arbitration agreement) in the context of:

- the arbitration rules (the institutional rules governing how the arbitration process is to be conducted);
- the curial law (the law providing the framework for the conduct of the arbitration and determining the powers of the court to supervise and support the arbitration); and
- the substantive law (the law governing the contractual obligations of the contract).

Enka v Chubb

In *Enka v Chubb*, the dispute arose out of a construction contract to construct a power plant in Berezovskaya, Russia. Notably, there was no express provision for the substantive law of the contract or the proper law of the arbitration agreement (the arbitration seat was London, England). A key issue in dispute was whether the proper law was Russian law or English law.

Lords Hamblen and Leggatt (with whom Lord Kerr agrees), delivering the majority judgment, decided that the proper law was English law.

- The proper law is determined in two steps. First, the law expressly or impliedly chosen. In the absence of an express choice, the courts presume that the implied choice is the substantive law since parties normally expect their contract to be governed by a single

system of law (except when doing so would invalidate the arbitration agreement but not when the arbitration seat is in a different country). Second, if there is no expressed/implied choice, then the law with which the arbitration agreement is most closely connected with.

- The majority decided that there was: (a) no express choice; and (b) no implied choice since parties could not agree to a substantive law. The majority then went on to decide the governing law of the main body and the arbitration agreement separately. The main body was closely connected to Russia and governed by Russian law. The arbitration agreement (in the absence of any choice), being most closely connected with the seat of the arbitration (London), was governed by English law.

It is interesting that despite upholding the "main contract" approach, the law lords bifurcated the determination of the governing law of the main body and the arbitration agreement to conclude that English law (being the law of the seat of arbitration) is the proper law.

Lord Burrows (with whom Lord Sales agrees), delivering the dissenting judgment, similarly upheld the "main contract" approach but concluded that the proper law of the arbitration agreement ought to be Russian law.

- There was no disagreement with the two steps for determining the proper law.

- The dissenting law lords found that the construction contract clearly hinted at Russian law as the substantive law. The proper law should be implied from the substantive law to be Russian law as well (unless this would invalidate the arbitration agreement). Yet, Russian law does not invalidate the arbitration agreement (it merely takes a narrower interpretation of the arbitration agreement). Hence, there was no reason to displace the presumption for Russian law to be the proper law.

Another interesting point is that the UK Supreme Court referenced the Singapore Court of Appeal case of *BNA v BNB* [2019] SGCA 84 ("**BNA v BNB**") with approval. In that case, Singapore's Court of Appeal similarly upheld the "main contract" approach.

BNA v BNB

In *BNA v BNB*, the substantive law of the contract was Chinese law and the proper law of the arbitration agreement was not expressly stated (although the arbitration agreement provided for arbitration administered by the Singapore International Arbitration Centre in Shanghai).

Steven Chong JA, delivering the judgment of the court, upheld the three-staged test for determining the proper law as set out in *BCY v BCZ* [2016] SGHC 249: (a) express choice; (b) implied choice (which can be implied from the substantive law); and (c) closest and most real connection to the dispute. This is similar to the two steps determination in *Enka v Chubb*.

Like *Enka v Chubb*, the parties in *BNA v BNB* did not make an express choice for the proper law. However, as the parties expressly provided for Chinese law as the substantive law, the presumption was that the parties had impliedly chosen Chinese law as the proper law. The choice of arbitration seat was not a sufficient reason to displace this presumption (and in any event, the arbitration seat was in Shanghai, China, where Chinese law applies as well).

What the Future Holds?

What is clear? The recent judgments from the highest courts of England and Wales, as well as Singapore, clarified that the "main contract" approach is favoured: where there is an express choice for the substantive law, the proper law normally follows the substantive law.

What is less clear? The application of the "main contract" approach is less certain where there is no express choice for the substantive law. Should the substantive law and proper law be construed separately (as by the majority)? Or should the construed substantive law be implied to be the proper law (as by the dissenting minority). Given the 3:2 decision in *Enka v Chubb*, the position may be re-visited by a different bench in future.

How We May Assist

As arbitration specialists, we are familiar with the latest arbitration developments and the conduct of arbitration proceedings. We advise clients on arbitration agreements, including the drafting of arbitration agreements to minimise subsequent controversies. We often assist clients in arbitration proceedings to achieve the most optimal commercial outcome.

To find out how we may assist, please do not hesitate to contact any of our lawyers.

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