The proper law of an arbitration agreement? Not always the proper law of the contract says the English Court of Appeal

Introduction

1. In the case of *Sulamérica Cia Nacional De Seguros S.A. v Enesa Engenharia S.A.* [2012] EWCA Civ 638 on 16th May 2012 the Court of Appeal has emphasised the significance of the choice of seat of arbitration. This could give rise to unexpected consequences where parties have assumed that the choice of governing law for the agreement also meant that the same law applied to the arbitration agreement.

2. The decision is not without controversy, and is likely to be criticised by some as being an example of excessive desire on the part of the English Courts to promote arbitration in London.

3. However, as we will explain, 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

4. The case concerns an insurance agreement between two sophisticated commercial parties relating to the construction of a power plant in Brazil. The insured claimed under the policy, but the insurers declined liability. 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.

5. The policy contained two potentially conflicting clauses; a London arbitration clause and an exclusive jurisdiction clause in favour of the courts of Brazil. Importantly, there is also an express choice of Brazilian law as the law governing the contract. Under Brazilian law, arbitration clauses can only be invoked with the consent of the other party; all arbitration is voluntary even if the contract stipulates binding arbitration.

6. 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. In response the insurers 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.

7. The Court of Appeal was faced with the question of whether to continue the injunction, which entailed an analysis of whether the arbitration agreement was governed by Brazilian law. If the insured's argument were correct, the reference to arbitration would be ineffective and the injunction would have to be discharged.

The Issues

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

    a. the express choice of the law of Brazil as the law governing the policy;
    b. the agreement that the courts of Brazil should have exclusive jurisdiction in respect of any disputes in connection with the policy;
    c. the close commercial connection between the policy and the state of Brazil; and
    d. 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.

9. By contrast, the insurers relied on the doctrine of separability to show that the arbitration agreement should be governed by the law of the seat, England.

The Court of Appeal's Reasoning

10. Moore-Bick LJ emphasised the importance of the doctrine of separability, which exists to insulate arbitration agreements from invalidating defects in the main contract. In finding that English law covered the arbitration agreement, he relied heavily on the *obiter dicta* by Longmore LJ in *C v D* [2007] EWCA Civ 1282, para 26 which suggest that the law of the arbitration agreement will have a closer connection to the law of the place of arbitration rather than the law of the contract.

11. Moore-Bick LJ inferred that the doctrine of separability can be used to separate the arbitration agreement from the main contract if the law of the contract would weaken the voluntary status of the arbitration agreement even where the main contract is not impaired. The arbitration agreement will then be governed by the law of the place of the arbitration. His two reasons for doing so are likely to be considered by some commentators are unconvincing or pragmatic:

    a. The choice of seat of arbitration in another country must suggest that the parties intended the law of that country to govern the arbitration.
    b. The fact that Brazilian law undermines the compulsory nature of the arbitration agreement suggests that the parties did not intend for Brazilian law to apply; they could have provided explicitly for voluntary arbitration.

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