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Governing law of the arbitration agreement: Importance of Sulamérica case reaffirmed where choice of seat was agreed without actual authority

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The December 2013 decision of the English Commercial Court (the Court) in Habas Sinai Ve Tibbi Gazlar Istihsal Andustrisi AS and VSC Steel Company Ltd [2013] EWHC 4071 (Comm) (Habas) summarised the guidance provided in Sulamérica Cia Nacional De Seguros S.A. and others v Enesa Engenharia S.A [2012] EWCA Civ 638 (Sulamérica) and Arsanovia Ltd v Cruz City 1 Mauritius Holdings [2013] 2 All ER 1 (Arsanovia) on determining the governing law of an arbitration agreement. In Habas, the Court applied those principles to determine the law of the arbitration agreement in a contract between a Turkish company and a Hong Kong company which provided for arbitration in London but no governing law of the substantive agreement or the arbitration agreement.

The Court reaffirmed the principles for determining the applicable law of the arbitration agreement which were set down in Sulamérica and considered in Arsanovia. The Court summarised the guidance provided by these cases, including the three stage test set out in Sulamérica that the proper law of the arbitration agreement is to be determined by undertaking a three stage enquiry: (i) whether the parties expressly chose the law of the arbitration agreement; (ii) whether the parties made an implied choice of the arbitration agreement; and (iii) in the absence of express or implied choice, the system of law with which the arbitration agreement has the "closest and most real connection". Applying these principles, the Court found that the applicable law of the arbitration agreement was the law of the country of the seat, i.e. English law. It dismissed the argument that the seat should not be relevant to the "closest connection" test, because Habas' agents had exceeded their actual authority when agreeing to London arbitration. The Court held that the applicable law of the putative agreement must be examined before any question of the validity should be considered. It refused to exclude consideration of the clause allegedly agreed in excess of authority when such clause was necessary to determine the applicable law. This required a consideration of the terms of the contract as made, rather than the authority with which it was made. The Court emphasised that as between principal and third party there is no difference between actual and ostensible authority and found that Habas' agents had ostensible authority to agree to the London arbitration agreement.

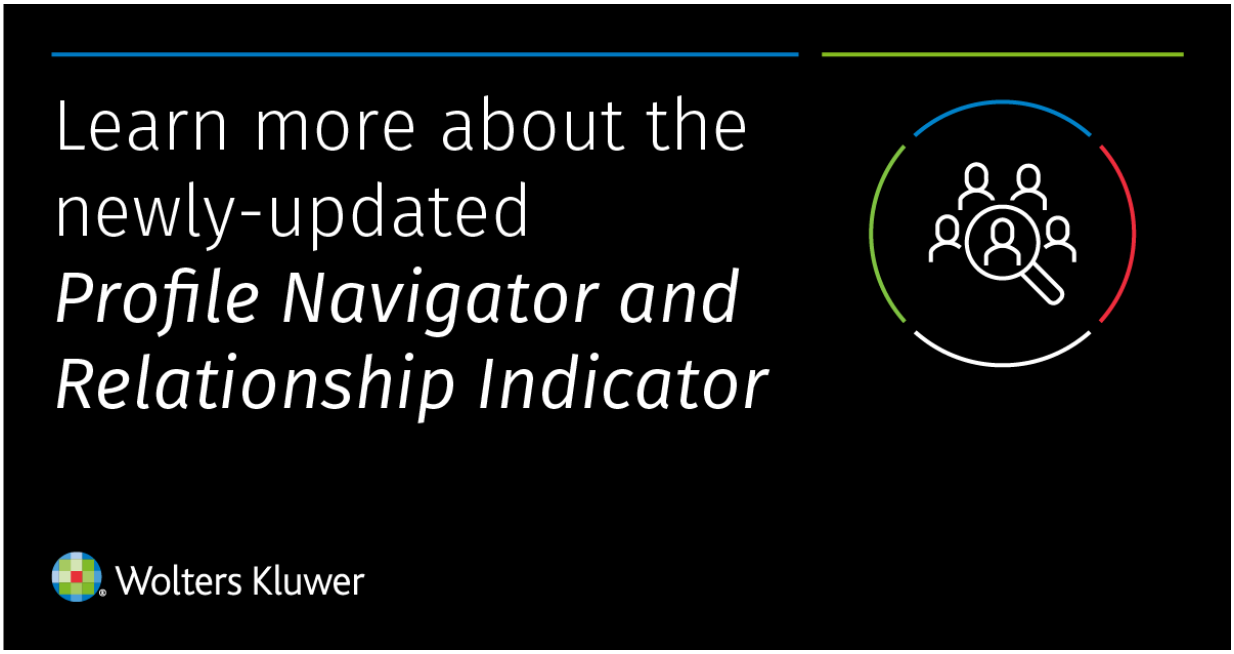
When referring to the third stage of the Sulamérica test, the Court added that the terms of the arbitration agreement may also indicate an implied choice of law. This observation appears to have been obiter dicta, as the Court did not apply it. It found that there was no express choice of law in

the matrix contract and that, following Sulamérica, the applicable law would be the country of the seat, being that with which the arbitration agreement had its closest and most real connection.

While the Court referred to the third stage of the Sulamérica test, the observation that that the terms of the arbitration agreement may also indicate an implied choice of law would seem to be more at home in the second stage of the test, i.e. the question of whether there is an implied choice of law. As noted by Moore-Bick LJ in Sulamérica, stage (ii) often merges into stage (iii), though as a matter of principle the stages should be embarked upon separately and in order. The Court's observation in Habas thus has the potential to muddy the waters surrounding the determination of the law of the arbitration agreement, not helped by the fact that the Court did not apply it to the case at hand.

As well as adding to uncertainty, the Court's observation seems to add little to the factors which the courts already consider as part of the first and second stages of the test. In Arsanovia, Andrew Smith J found that the terms of the arbitration agreement which excluded parts of the Indian Arbitration and Conciliation Act 1996 demonstrated a mutual intention of the parties to choose the law of India as the law of the arbitration agreement.

The outcome of the application of the three stage test laid down in Sulamérica therefore remains unpredictable. It will depend on whether there is an express choice of law of the matrix contract; whether there is a choice of seat in the arbitration agreement (and whether this is different to the express choice of law of the matrix contract), and whether there are any other "sufficient factors" which may displace an attempt to imply a choice of law on the basis of the chosen seat and lead to application of the third stage (the "closest connection" test). The case again highlights the importance of expressly including a governing law clause in the arbitration agreement in international contracts.



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