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The Ghost of the Governing Law Returns: Lex Arbitri v. Curial Law in India

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On 14 February 2014, the Supreme Court of India (**SCI**) in *Enercon India v. Enercon GMBH* [Civ. App. 2086/7 of 2014] (**Enercon**) found occasion to revisit issues in connection with potential laws that govern an arbitration agreement. The impugned arbitration agreement contained the following clause:

> 18. DISPUTES AND ARBITRATION
> 18.1 * * *
> 18.2 * * *
> 18.3 A proceedings in such arbitration shall be conducted in English. **The venue of the arbitration proceedings shall be in London.** The arbitrators may (but shall not be obliged to) award costs and reasonable expenses (including reasonable-fees of counsel) to the Party (ies) that substantially prevail on merit. **The provisions of Indian Arbitration and Conciliation Act, 1996 shall apply.** (emphasis added)

Let us first keep in mind that there are three laws that are potentially applicable to an arbitration agreement:
(1) The law of the arbitration agreement (**governing law**)
(2) The proper law of the contract (**substantive law**)
(3) The law of the seat of arbitration

The ideal arbitration clause will specify each of the above. However, if the governing law remains undefined, according to the decision of the SCI in *NTPC v Singer* [AIR 1993 SC 998], the substantive law is normally the governing law as well. However, in exceptional circumstances and if there is no substantive law defined, the law of the seat will be deemed to be the governing law as the law bearing the "closest connection" to the dispute. This position is slightly different from that in the UK where as per the three-stage test laid down in *Sulamerica v. Enesa* [(2012) EWCA Civ 638] (**Sulamerica**) the governing law is either (i) expressly chosen; (ii) impliedly chosen; and (iii) in the event it is neither expressly nor impliedly chosen, it is the law of the seat of the arbitration. Although the court took note of the fact that an express choice of substantive law (Brazil) is a persuasive indicator of governing law, it went on to hold that the identification of the seat as

London is a more impressive factor in arriving at the conclusion that the English Arbitration Act would have the closest connection and held that the governing law would be English law. This position was confirmed by the English Commercial Court in *Habas Sinai v. VSC* [(2013) EWHC 4071], where the court, in a dispute where neither the substantive law nor the governing law was specified, applied the closest connection test to conclude that the law of the seat would be the law applicable to the arbitration agreement.

The difference, therefore, in the two positions is that when a seat and a substantive law is identified in the absence of a governing law, courts in India will lean towards holding that the substantive law bears the closest connection whereas the courts in England will lean towards holding that the law of the seat bears the closest connection. In other words, Indian courts will look for the closest and most real connection to the dispute, while English courts will look for the closest and most real connection to the seat of the arbitration to ensure the procedure is effective.

The SCI in *Enercon* tried to apply the closest connection test inversely. The controversy arose because the dispute resolution clause clearly designated Indian law as the substantive law. It also made the Indian Arbitration and Conciliation Act, 1996 (**Indian Arbitration Act**) applicable. However, the clause stated that the ***venue*** for the arbitration proceedings would be London. The court was asked to consider if the word 'venue' was intended to be used interchangeably with 'seat' or 'place' of arbitration or whether London was designated as only the venue of the hearings as against the 'seat' or 'place' of arbitration.

This issue is slightly more complicated because it also involves a question of the jurisdiction of the courts because of the lack of clarity with regard to the curial law applicable. Most practitioners experienced in international commercial arbitration in Indian courts would try to advise their clients to draft the arbitration clause in a way to oust the jurisdiction of the Indian courts, both for reasons of inconsistent judgments as well as long drawn proceedings. As a result, there was an emerging practice to have Indian law as the applicable substantive law, the Indian Arbitration Act as the applicable governing law (by virtue of *NTPC v Singer*) but have the arbitration seated in London to ensure procedural efficiency by yielding supervisory jurisdiction to English courts. The judicial treatment of such a situation was seen in *Arsanovia v. Cruz City* [(2012) EWHC 3702] where the applicable substantive law was Indian, LCIA was administering the arbitration and London was the seat of arbitration. The English courts applied the provisions of the Indian Arbitration Act as the governing law to determine whether or not the tribunals had the substantive jurisdiction to render the awards challenged under Section 67 of the English Arbitration Act.

The SCI in *Enercon* heavily relied upon the decisions of *Naviera Amazonica v. Compania Internacional* [(1988) 1 Lloyd's Rep 116], C v. D [(2007) EWHC 1541] and the EWHC decision in *Sulamerica* [(2012) EWHC 42] to arrive at the conclusion that since the governing law was Indian and the Indian Arbitration Act was expressly made applicable, all three laws with potential applicability in an arbitration dispute were Indian and therefore, it was only reasonable that parties intended New Delhi be the seat of arbitration vesting the courts in India with exclusive supervisory jurisdiction. The court seems to have assumed that by expressly making the Indian Arbitration Act applicable, Indian law was designated as both the governing law and the curial law. This decision stems from 2 basic elements of reasoning- (1) the word 'venue' was used in reference to London; and (2) an "absurd" situation would arise because "*the Indian Arbitration Act, 1996 would apply to the process of appointment under Section 11; English Arbitration Act, 1996 would apply to the arbitration proceedings (despite the choice of the parties to apply Chapter V to the Part I of the Indian Arbitration Act, 1996); challenge to the award would be under English Arbitration Act,*

1996 and not under the Part I of the Indian Arbitration Act, 1996; [and the] *Indian Arbitration Act, 1996 (Section 48) would apply to the enforcement of the award.*"

However, this "absurd" situation is almost identical to the facts in *Arsanovia*, the only difference being that in *Arsanovia*, the dispute resolution clause specifically excluded the applicability of the curial provisions of the Indian Arbitration Act ["*Notwithstanding the above, the Parties hereto specifically agree that they will not seek any interim relief in India under the Rules or under the Arbitration and Conciliation Act, 1996 (the "Indian Arbitration Act"), including Section 9 thereof. The provisions of Part 1 of the Indian Arbitration Act are expressly excluded*"] while the clause in *Enercon* simply stated the applicability of the Indian Arbitration Act. The impact of this is an uncertainty with respect to which of the two situations constitutes the rule and which of the two stands as an exceptional situation to be distinguished from general practice with regard to the conflict of laws. This is further amplified by the fact that the court makes no reference to the Court of Appeal decision in *Sulamerica*, the decision in *Arsanovia* or even the decision of the SCI in *NTPC v Singer*.

In addition, the court states that the parties "*would not have intended to have created an exceptionally difficult situation, of extreme complexities*" by designating London as the seat of arbitration. Ironically, it is the complexities that arise out of the applicability of Part I of the Indian Arbitration Act (interim relief, discovery, patent illegality as a part of public policy) that encourages practitioners to recommend that the seat of arbitration be outside India. If that was indeed the intention of the parties that has been overlooked by the court, it will have serious implications on the drafting of the arbitration clause in commercial contracts where the applicable substantive law is Indian law. However, it must be conceded that there does seem to exist a reason to believe that in *Enercon* London was designated only as a convenient place for hearings by virtue of the use of the word 'venue'.

This judgment may have a negative impact on the choice of law in international commercial arbitrations due to smudging of the distinction between the *lex arbitri* and the curial law. But the good thing is that this issue seems to have been revisited by the court as a result of the pro-arbitration stance of the Indian courts in, if we may call it so, the post-BALCO era of Indian arbitration. We make this observation in light of the first part of the *Enercon* judgment which refers the dispute to arbitration in order to give effect to the "common-sense" intention of the parties in spite of vehement allegations that the arbitration agreement was contained in a contract that was not concluded and that the arbitration clause was unworkable. The SCI emphasized on the necessity of the concept of separability of the arbitration agreement saying that the issues with respect to the conclusion of the contract "*pale into insignificance*" in the face of the dispute resolution clause. The SCI defined the role of courts in the arbitral process as players that "aid and support" it and work towards its progress.

Although lack of clarity continues to prevail with respect to governing law, the arbitration community can afford to heave a sigh of relief since India seems to be fast making its way towards becoming an arbitration friendly jurisdiction.

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