Kluwer Arbitration Blog

Enka v Chubb [2020] UKSC 38: Bringing the Validation Principle Into the Light

Steven Lim (39 Essex Chambers) · Wednesday, December 16th, 2020

Much has been written about the UK Supreme Court's decision in *Enka v Chubb* [2020] UKSC 38 ("***Enka***") including on the blog. Those familiar with the judgment will know the Supreme Court decision was split 3 – 2 and the majority upheld the Court of Appeal's decision but on different grounds. These divisions may give the appearance the law remains as confusing as it was. However, the Supreme Court decision is much less divided than it appears. The majority and the minority agreed on more than they disagreed. It is important to note all five judges agreed an express choice of the main contract law would, save for the validation principle,[1)] be an express or implied choice of law for the arbitration agreement as well. This settles the position in English law for the majority of cases where the main contract contains an express choice of law clause.

One should also bear in mind the split in the Court arose on the uncommon facts of *Enka:* there was no express choice of law in the main contract, leading to differences on two primary issues:

- Implication of the main contract law; and
- The principle to be applied to the determination of the law with the closest connection at stage three of the "express law-implied law-closest connection" three-stage test.

The Court did not differ on the answer had the main contract contained an express choice of law clause.

This post focuses on the Court's express recognition of a validation principle in the determination of the law of the arbitration agreement.

Bringing the validation principle into the light

Enka is the first decision in the English Courts to expressly recognise the application of a validation principle to the determination of the law of the arbitration agreement. All five judges agreed on this.

The Supreme Court framed the validation principle as a principle of English contractual interpretation dating back to the 17th century, expressed in the Latin maxim "verba ita sunt intelligenda ut res magis valeat quam pereat" (the "**ut res magis principle**") *i.e.* the contract

should be interpreted so that it is valid rather than ineffective. (*Enka*, [95])[2] The Court recognised the principle applied if a putative governing law, where none had been expressly chosen, would render all or part of the agreement ineffective.

The Court explained several earlier cases, including *Hamlyn & Co v Taliker Distillery* [1894] AC 202 and *Sulamérica Cia Nacional de Seguros SA and others* v *Enesa Engelharia SA and others* [2013] 1 WLR 102 ("***Sulamérica***"), can be understood by way of the validation principle, in that the Courts had applied the choice of law which validated and gave effect to the arbitration agreement.

The Court explained the validation principle was purposive:

> The principle that contracting parties could not reasonably have intended a significant clause in their contract, such as an arbitration clause, to be invalid is a form of purposive interpretation, which seeks to interpret the language of the contract, so far as possible, in a way which will give effect to – rather than defeat an aim or purpose which the parties can be taken to have had in view. (*Enka*, [106])

This rationale is in line with the validation principle implied in the scheme of the New York Convention[3] to uphold and give effect to arbitration agreements. While the Court explained the validation principle in English law terms, the majority recognised the New York Convention encapsulates a similar principle in the choice of law rule in Articles V(1)(a) and II(3). (*Enka*, [128] to [131])

Notably, the Supreme Court took a broad approach to the application of the validation principle. It not only applies when a putative choice of law would invalidate the arbitration agreement, it also applies where there is a serious risk, but not a certainty, a putative law would defeat or frustrate the purpose of the arbitration agreement. The majority of the Court said the principle extends to a failure to recognise that arbitration is chosen as a one stop method of dispute resolution – *i.e.* the validation principle favours an expansive interpretation of the arbitration agreement, in cases of doubt, to encompass disputed claims. (*Enka*, [107] to [108]) The majority and minority were divided on whether the validation principle applies to the scope of the arbitration agreement as opposed to its validity. This is discussed further below.

In defining the validation principle, the Court said it could not improve on the formulation of Moore-Bick LJ in *Sulamérica* that commercial parties are generally unlikely to have intended a choice of governing law for the contract to apply to an arbitration agreement if there is "at least a serious risk" that a choice of that law would "significantly undermine" that agreement. (*Enka*, [109])

Validation principle applies to scope and validity of the arbitration agreement

As noted above, the majority was of the view the validation principle applied to the scope of the arbitration agreement, in addition to its validity. Lords Burrows and Sales departed from the majority on this – they did not agree the same choice of law rules (and hence the validation

principle) applies to both the validity of the arbitration agreement and to its scope.

The majority found the general approach in conflict of laws, adopted by both the common law and the EU Rome I Regulation, is to treat the validity and scope of a contract (as well as other issues, such as the consequences of breach and ways of extinguishing obligations) as governed by the same applicable law. This makes good sense, not least because the boundary between issues of validity and scope is not always clear. It is logical to apply the law identified by the conflict rules prescribed by article V(1)(a) of the New York Convention, enacted in England in section 103(2)(b) Arbitration Act 1996 ("**Arbitration Act**"), to questions about the scope or interpretation of the arbitration agreement as well as disputes about its validity.[4)]

The majority's view is supported by the scheme of the New York Convention. As the majority recognised, the New York Convention is to be interpreted to apply the same conflicts rule to Art II(3) of the Convention, on recognition of arbitration agreements, as in Article V(1)(a) New York Convention (*Enka*, [130])[5)] *i.e.* the same choice of law rule should apply pre and post-award. Article II(3) of the New York Convention (enacted as section 9(4) Arbitration Act) requires the court to recognise and enforce an arbitration agreement (and to stay litigation brought in breach of the arbitration agreement) unless the agreement is "null and void, inoperative or incapable of being performed". While not express, the scope of the arbitration agreement must form part of the court's enquiry, at least on a *prima facie* basis – if the arbitration agreement patently does not cover the dispute then the court is not required to stay the litigation before it in favour of arbitration. It is clear the scheme of the Convention requires the same governing law (and the same means of determining the governing law) to be applied both to scope and to validity.

Validation principle and the law of the closest connection

The minority did not agree with the default application of the law of the seat as the law with the closest connection to the arbitration agreement – they preferred the application of the law of the main contract, even if determined as a rule of law by the closest connection – with the application of the validation principle displacing the main contract law, if necessary. (*Enka*, [285]) The majority left open whether the validation principle can apply to displace the law of the seat as the law with the closest connection. (*Enka*, [146])

The validation principle said to be embedded in the New York Convention, most notably associated with Gary Born's work,[6)] is said to operate at the implied choice stage, favouring the implication of a law validating the arbitration agreement, to give effect to the parties' agreement to arbitrate. The application of the default choice of the law of the seat law, or of the closest connection, should therefore not arise in most cases.

All five judges in the Supreme Court agreed there is no sharp distinction between an implied choice and a default positive rule of law. (*Enka*, [37], [256] and [282]) A more expansive approach to the application of the validation principle at the implication stage[7)] may obviate the debate seen in *Enka* over the default choice of the law of the seat as the law with the closest connection and whether the validation principle applies at that stage.

Consistency with international law and legislative policy

The Supreme Court's decision in *Enka* is to be lauded for the majority's sophisticated consideration of the scheme of the New York Convention and other international instruments, as well as sections of the Arbitration Act giving effect to the New York Convention. (*Enka*, [125] to [141])

The Court's careful treatment of the validation principle can be contrasted with the Singapore High Court decision in *BNA* v *BNB* [2019] SGHC 142 ("***BNA HC***"), in which the Court rejected the application of the validation principle in Singapore law as impermissibly instrumental, inconsistent with the parties' intention, unnecessary because of the ut res magis principle and inconsistent with Article V(1)(a) of the New York Convention, discussed by the author in an earlier post. (*BNA HC*, [53], [55], [62] and [65])

The validation principle gives effect to the parties' agreement to arbitrate and is derived from the choice of law principles and pro-enforcement policy in Article V(1)(a) and Article II of the New York Convention. The majority's decision in *Enka* recognised this and emphasised the importance of an internationally consistent approach to the arbitration agreement proper law, and for a uniform approach across national courts. (*Enka*, [136]) This is a welcome alignment of English law with the transnational approach to the proper law of the arbitration agreement.

References

?1 The majority thought another excepting circumstance might be where the law of the seat provides, in the absence of an express choice, the arbitration agreement will also be treated as governed by the law of the seat (*e.g.* Swedish Arbitration Act, section 48; Arbitration (Scotland) Act 2010, section 6).

?2 Staughton LJ in *Lancashire County Council v Municipal Mutual Insurance Ltd* [1997] QB 897, 910.

?3, ?6 *See* Gary Born, *The Law Governing International Arbitration Agreements: An International Perspective* (2014) 26 SAcLJ 814 at [27], [56] and [59].

?4 The majority also referred to the Restatement (Third) US Law of International Commercial and Investor-State Arbitration (which applies the same rule to scope as well as validity) – *Enka*, [139] and [140].

?5 Applied in section 103(2)(d) Arbitration Act; Article 36(i)(a)(iii) Model Law.

?7 *Enka*, [245] per Lord Burrows – insufficient weight had been given to the implied choice of the parties in the past.

This entry was posted on Wednesday, December 16th, 2020 at 7:18 am and is filed under Common Law, England, English courts, Law governing the arbitration agreement, New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Validation
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.