UK SUPREME COURT PROVIDES FURTHER GUIDANCE ON THE GOVERNING LAW OF AN ARBITRATION AGREEMENT: KABAB-JI SAL (LEBANON) V KOUT FOOD GROUP (KUWAIT)

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International Arbitration Alert

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Following the decision in *Enka Insaat ve Sanayi A.S. v OOO Insurance Company Chubb [2020] UKSC 38 (Enka)* on which we previously reported, the UK Supreme Court has provided further helpful clarification as to the approach to be adopted when the court is required, in the absence of an express choice, to decide what is the governing law of an agreement to arbitrate—this time, in the context of a party's attempt to enforce an arbitration award.

BACKGROUND TO THE DISPUTE

A dispute arose between a Lebanese business in the restaurant industry, Kabab-Ji, and a Kuwaiti company, Al Homaizi, with which Kabab-Ji had entered into a franchise development agreement (FDA). The FDA gave Al Homaizi the right to operate a franchise using Kabab-Ji's restaurant concept in Kuwait for ten years. The FDA contained an English governing law clause and an agreement to arbitrate, which provided for arbitration seated in Paris (the Arbitration Agreement). Crucially, the Arbitration Agreement did not specify the law which governed the parties' agreement to arbitrate. In 2005, Al Homaizi became a subsidiary of Kout Food Group (KFG) following a corporate reorganisation. Kabab-Ji referred the dispute to arbitration in Paris against KFG under the Rules of the International Chamber of Commerce.

KFG argued that it was not a party to the FDA or the Arbitration Agreement therein. The arbitrators in Paris made an award in favour of Kabab-Ji (the Claimant), deciding that French law (the law of the seat) determines whether KFG was bound by the Arbitration Agreement. The tribunal found that under French law, KFG was a party to the Arbitration Agreement and awarded damages and costs against KFG totalling about US$ 6.7 million. Kabab-Ji brought proceedings in the English Commercial Court to recognise and enforce the award.

DECISIONS OF THE LOWER COURTS

Burton J at first instance decided that the law governing the validity of the Arbitration Agreement was English law and KFG had not become a party to the Arbitration Agreement applying English law principles.

The Court of Appeal dismissed the Claimant's appeal, finding that English law governed the Arbitration Agreement and as a matter of English law, in the absence of written consent as required by the terms of the FDA or any matters capable of giving rise to an estoppel, KFG could not have become a party to the FDA and hence

the Arbitration Agreement. The Court of Appeal gave summary judgment in favour of KFG, refusing recognition and enforcement of the Award.

The Claimant was given permission to appeal on five grounds, including the issue of which law governs the Arbitration Agreement.

As we reported, the Supreme Court in *Enka* previously decided that where there is no express provision in relation to the governing law of the parties' agreement to arbitrate, an express choice of governing law in the main contract will generally be considered to represent an implied choice of law applicable to the agreement to arbitrate (unless there are particular factors to the contrary, such as invalidity of the arbitration clause). However, the conclusions in *Enka*, in which the court was applying English common law rules for resolving conflicts of law, were not directly applicable in this case, which related to the enforcement of an award that had already been issued.

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Relevant Statutory Provisions

Article V of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the Convention) sets out a limited list of grounds on which the recognition and enforcement of an award may be refused.

Article V(1)(a) of the Convention applies where: “The parties to the [arbitration agreement], under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made”.”

Section 103 of the Arbitration Act 1996 (the Act) replicates Article V of the Convention.

The only ground for resisting enforcement of the award available to KFG was the alleged invalidity of the Arbitration Agreement, relying on Article V(1)(a) of the Convention (replicated in section 103(2)(b) of the Act).

In construing the relevant clause in the FDA, the court found that it was a “typical governing law clause” providing that “this Agreement” shall be governed by the laws of England, sufficient to denote all the clauses in the contract, including the Arbitration Agreement.

The Claimant advanced two arguments in support of its assertion that the Arbitration Agreement was governed by French law, the law of the seat. In the first, it asserted that, since the Arbitration Agreement refers to “principles of law generally recognised in international transactions” (agreed by the parties to be a reference to the International Institute for the Unification of Private Law (UNIDROIT): Principles of International Commercial Contracts), when read together with the governing law clause of the contract (English law), there was no “sufficient indication” of the law governing the validity of the Arbitration Agreement, and therefore the default rule under Article V(1)(a) and s.103(2)(b) of the Act should apply (i.e., the law of the country where the award is made should apply), and the applicable law is therefore the law of the seat, French law. The court found this would lead to an absurd result whereby if parties choose a governing law supplemented by additional principles, their arbitration agreement would be governed by a system of law they did not choose. Further, the court stated that the relevant governing law clause relied upon concerned what rules of law were to be applied in deciding the substantive issues, not which law is to be applied to the question of the validity of the Arbitration Agreement.

The second argument relied on by the Claimant and rejected by the court, was based on the "validation principle", according to which contractual provisions, including any choice of law provision, should be interpreted so as to give effect to, and not defeat or undermine, the validity of an agreement to arbitrate. The court held that this was an attempt to extend the validation principle beyond its proper scope, since the principle presupposes that an agreement has already been made to submit disputes to arbitration: "It is not a principle relating to the formation of contracts which can be invoked to create an agreement which would not otherwise exist."

The Supreme Court therefore endorsed the conclusion of Burton J and the Court of Appeal that the law governing the question of whether KFG became a party to the Arbitration Agreement is English law. The court held that under English law there is no real prospect of a court finding that KFG became a party to the Arbitration Agreement, and that the Court of Appeal was right to give summary judgment refusing recognition and enforcement of the award.

COMMENT

Certainty as to the governing law of an agreement to arbitrate is highly desirable since any confusion as to the governing law could have serious consequences in terms of the arbitral tribunal's jurisdiction, the validity of the agreement to arbitrate and the enforceability of any award.

Whilst the decision in the *Kabab-Ji* case is helpful in extending the Supreme Court's approach in *Enka* to the enforcement context, parties should, wherever possible, expressly provide which law governs their agreements to arbitrate in addition to providing for an express choice of the substantive law governing the contract, and designating the seat.

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