

Liability Insurance in International Arbitration: Choice of Law Issues in ‘Bermuda Form’ Arbitrations

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In the mid-1980s the excess casualty insurance market in the USA collapsed to a very substantial extent. A number of insurance companies rose from the ashes, fuelled in part by capital from large US manufacturing companies. Two of these companies, ACE and XL, were based in Bermuda and began to write insurance on a freshly-drafted and novel policy form which rapidly became known as the ‘Bermuda Form’. The Bermuda Form has been through a number of revisions¹ and is now one of the principal policy forms used in high-level excess liability insurance policies purchased by large US corporations for the purposes of insuring against the risk of catastrophic liabilities, for example the manufacture of a product which gives rise to mass tort litigation or a refinery explosion which causes substantial property damage and personal injury.

Insurance policies written on the Bermuda Form have a distinctly international flavour. The policyholder and the insurers are often based in different countries, the policy includes an express choice of New York law (with certain modifications), and invariably provides for disputes to be settled by arbitration, usually in England, sometimes in Bermuda. The flavour of the contractual provisions can

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¹ Currently, ACE writes on version 5 of their form and XL on version 4. Many other companies now write high-level liability insurance on versions of the Bermuda Form. The companies include Swiss Re, Zurich, Gerling, Starr Excess (an AIG subsidiary) and others. Policies have been written on the Bermuda Form since 1986. For a general introduction, see Dolin and Posner, ‘Understanding the Bermuda Excess Liability Form’ in (1998) 1(4) *Journal of Insurance Coverage* (Autumn) 68 and Masters, ‘Ace and XL: A New “Batch” of Coverage Issues’ in (1999) 9(1) *Coverage* (January/February) 24).

be gleaned from the 'Construction and Interpretation' and 'Arbitration' clauses in one current version of the Bermuda Form.² The former provides:

This Policy, and any dispute, controversy or claim arising out of or relating to this Policy, shall be governed by and construed in accordance with the internal laws of the State of New York, except insofar as such laws:

- (1) may prohibit payment in respect of punitive damages hereunder;
- (2) pertain to regulation under the New York Insurance Law or regulations issued by the Insurance Department of the State of New York pursuant thereto, applying to insurers doing insurance business, or issuance, delivery or procurement of policies of insurance, within the State of New York or as respects risks or insureds situated in the State of New York; or
- (3) are inconsistent with any provision of this Policy;

provided, however, that the provisions, stipulations, exclusions and conditions of the Policy are to be construed in an even-handed fashion as between the Insured and the Company; without limitation, where the language of this Policy is deemed to be ambiguous or otherwise unclear, the issue shall be resolved in the manner most consistent with the relevant provisions, stipulations, exclusions and conditions (without regard to authorship of the language, without any presumption or arbitrary interpretation or construction in favor of either the Insured or the Company or reference to the 'reasonable expectation' of either thereof or to *contra proferentem* and without reference to parol or other extrinsic evidence). To the extent that New York law is inapplicable by virtue of any exception or proviso enumerated above or otherwise, and as respects arbitration procedure pursuant to Condition N, the internal laws of England and Wales shall apply.

The arbitration provision (Condition N) provides that:

Any dispute, controversy or claim arising out of or relating to this Policy or the breach, termination or invalidity thereof shall be finally and fully determined in London, England under the provisions of the Arbitration Acts of 1950, 1975 and 1979 and/or any statutory modification or amendments thereto, for the time being in force, by a Board composed of three arbitrators to be selected as follows ...³

It might at first sight seem somewhat unusual for a standard-form insurance policy to provide for disputes under a contract governed by New York law to be arbitrated in London. The historical background to the Bermuda Form provides the answer. The insurance companies were anxious to avoid their disputes being resolved by US courts which were perceived, rightly or wrongly, as too pro-assured. Arbitration was viewed as potentially more efficient and less expensive than US court litigation. The insurance companies typically appointed English barristers as their party-appointed arbitrators. This was perhaps because London arbitration offered the industry the opportunity to have their new policy form interpreted by arbitrators who would come to the policy form afresh and without any preconceptions that might be derived from extensive involvement in

² XL's form XS 004.

³ The clause then provides in detail for the manner of appointment of arbitrators and for various other matters relating to the arbitration.

insurance disputes in the USA. By providing for New York law in confidential London arbitration, the chances of the form being subjected to interpretation by the courts (either in the USA or England) would be minimized if not negated. In particular (as discussed later in this article) appeals to the English courts on issues of law would not be possible, since no question of English substantive law would ever be involved. On the other hand, buyers of insurance (envisaged at the outset as being large US corporations) were not required to submit to English law as the substantive law of the contract. Instead, the policy provided for the law of New York; a state whose insurance law was perceived as less pro-assured than others, but was still more benevolent to assureds than English law in certain respects.⁴

This article concerns some of the consequences of this international character of Bermuda Form arbitrations, and the respective roles that the various systems of law may have over questions that arise in the course of resolving a dispute. Since the important demarcation is normally between English law, which is the centre of gravity of the dispute resolution provisions, and New York law, which is the centre of gravity of the provisions of substantive law, reference will mostly be to these systems of law. But it should be remembered that some versions of the form have provided for Bermuda arbitration, so that reference to 'England' and 'English law' should sometimes be read as references to 'Bermuda' and 'Bermudian law'.

There are six main areas in which it may be necessary to identify a governing law for the purposes of a dispute under the Bermuda Form. First, if the question arises whether there is a valid arbitration agreement, or whether a particular dispute is covered by it, it is necessary to identify the law governing the arbitration agreement. Secondly, in the course of the arbitration, it may be necessary for the tribunal to identify the legal rules and principles which govern its conduct of the arbitration, referred to here as the 'internal procedural law' of the arbitration. Thirdly, it may be necessary to identify the system of law governing judicial supervision of the arbitration process, and the courts having jurisdiction to supervise the process. That would happen, for instance, if problems arose concerning the appointment of an arbitrator, or there was some challenge to the arbitration tribunal's conduct of the proceedings. It is referred to herein as the 'curial law'. Fourthly, it may be necessary to identify the legal rules that govern any substantive issues of conflict of laws that arise in the course of the arbitration proceedings, that is to say the system which dictates the choice of law rules to be applied by the tribunal. We refer to that as the 'law governing choice of law'. Fifthly, it will be necessary to identify the legal rules governing the dispute. We refer to that as the 'applicable substantive law'. Sixthly, it may be necessary to consider the legal rules which governed the legal proceedings out of which the insured's liability arose. We refer to that as the 'law governing the underlying claim'.

⁴ Notably in the law relating to non-disclosure and misrepresentation.

This taxonomy is complicated enough as it is, but even so it might be argued that it is technically incomplete. At least in England – where the elaboration of choice of law *rules* is taken further than it characteristically is in the USA – writers have identified a number of other systems of law which may apply in an arbitration.⁵ For present purposes, at least, the division set out above is sufficient.

I. THE LAW GOVERNING THE ARBITRATION AGREEMENT

Most legal systems – including all those likely to have a bearing on a dispute under the Bermuda Form⁶ – now recognize the doctrine of the ‘separability’ of an arbitration clause. Under this doctrine, an arbitration clause is treated for various contractual purposes as if it were separate from the rest of the contract in which it is physically embedded. The result is that the arbitration agreement may be valid even if the contract in which it is found is void or voidable (for instance because of misrepresentation, or because it infringes public policy). The arbitration agreement may survive the termination of the substantive contract (for instance, its frustration). It also follows that the validity and interpretation of the arbitration agreement is not necessarily governed by the same legal rules as govern the substantive provisions of the contract. Where, therefore, some question arises as to the validity or meaning of the arbitration agreement, it becomes necessary to identify the law governing that arbitration agreement.

Under the Bermuda Form there are two obvious candidates: New York law, as the primary applicable law for the substantive parts of the policy,⁷ or English law as the law governing the procedural aspects of the arbitration.⁸ How the choice between these two candidates is approached will depend on where the issue arises, since it depends on the conflict of laws rules of the forum deciding the question. An English court, therefore, will apply English law conflict of laws rules.⁹ An arbitration tribunal appointed under the Bermuda Form would also probably be bound to apply English choice of law rules in deciding any question as to its jurisdiction. To do otherwise would make little sense, since either party would have the right to challenge the tribunal’s decision on such an issue before

⁵ See Mustill and Boyd, *Commercial Arbitration* (2nd edn., Butterworths, London, 1989), pp. 60–62, Mustill and Boyd, *Commercial Arbitration: 2001 Companion* (Butterworths, London, 2001), p. 122; cf. Dicey and Morris, *The Conflict of Laws* (Collins (ed.), 13th edn., Sweet & Maxwell, London, 2000), vol. 1, p. 593 (hereafter ‘Dicey and Morris’).

⁶ England: see Arbitration Act 1996, s. 7 and (at common law) *Bremer Vulkan Schiffbau und Maschinenfabrik v. South India Shipping Corp. Ltd* [1981] AC 909, *Harbour Assurance Co (UK) Ltd v. Kansa General Insurance Co. Ltd* [1993] QB 701. Bermuda: UNCITRAL Model Law, art. 16(1). For the position under the Federal Arbitration Act see *Prima Paint Corp v. Flood & Conklin Mfg Co* 388 U.S. 395 (1967).

⁷ See *infra*.

⁸ See *infra*.

⁹ English common law, since the Rome Convention, which generally applies to questions concerning choice of law in contracts, is expressly inapplicable to arbitration and jurisdiction clauses: Art. 1(2)(d). Contracts (Applicable Law) Act 1990 simply gave the Convention the ‘force of law’, including this exclusion, so that one is left to rely on the common law rules.

the English court,¹⁰ which will naturally apply its own conflict of laws rules. But if an issue as to the validity of the arbitration clause arises in, say, a US court – perhaps in the context of an application to stay proceedings brought against a Bermuda Form insurer under the Federal Arbitration Act¹¹ – the US court typically would apply its own conflict of laws rules to decide whether the arbitration agreement is valid and enforceable and whether a particular dispute falls within it.¹² In that sense, there is no definitive answer to the question ‘What law governs the arbitration agreement?’, since the way that question is approached will depend on where it arises. In what follows we consider the English law rules, since it is those that would be applied by any arbitration tribunal called upon to decide its own jurisdiction.

In *XL v. Owens Corning*¹³ Toulson J held that the arbitration agreement in the Bermuda Form is governed by English law. He therefore applied English law, as the putative proper law, to decide whether the arbitration agreement was valid. As a result, he was prepared to uphold an anti-suit injunction granted to XL to restrain the conduct of proceedings against it in Delaware. (Had he concluded that the arbitration agreement was governed by New York law it would have been arguable that the arbitration agreement in that case would not have been regarded as formally effective.)¹⁴ Toulson J relied principally on two factors in reaching his conclusion. First, he seems to have thought that *dicta* of Lord Mustill in *Channel Tunnel Group Ltd v. Balfour Beatty Construction Ltd*¹⁵ suggested that it was more likely that the proper law of the arbitration agreement would mirror the procedural law governing the arbitration than that it would track the substantive law governing the rest of the contract in which it is contained. Since the procedural law governing arbitration under the Bermuda Form is English law, he thought it likely that the arbitration agreement would also be governed by English law. Secondly, he was impressed by the express reference in the Bermuda Form to the arbitration being conducted ‘under the provisions of the Arbitration Act 1996’.

Both these conclusions are questionable, at least as a matter of English law.¹⁶ The passage from Lord Mustill’s speech in *Channel Tunnel* on which Toulson J relied reads as follows:¹⁷

It is now firmly established that more than one system of law may bear upon an international arbitration. Thus, there is the proper law which regulates the substantive rights and duties of the

¹⁰ Arbitration Act 1996, s. 67. Under the Arbitration Act 1996 a tribunal may, and normally will, decide any issue as to its own jurisdiction that arises in the course of the arbitration: *ibid.* ss. 30, 31. However, its decision is never conclusive, but always subject to judicial challenge.

¹¹ 9 USC §§ 201, 216.

¹² *ibid.* § 2 (validity) and § 3 (scope).

¹³ [2000] 2 Lloyd’s Rep. 500.

¹⁴ *Kahn Lucas Lancaster Inc v. Lark Int’l Ltd* 186 F.3d 210 (2d Cir. 1999). The problem is a notorious one concerning what is required for an agreement to be ‘in writing’ for the purposes of the New York Convention of 1958.

¹⁵ [1993] AC 334.

¹⁶ An appeal was withdrawn when Owens Corning entered Chapter 7 bankruptcy in the USA. Toulson J’s decision would be persuasive but not binding in England.

¹⁷ *Channel Tunnel Group Ltd.*, *supra* n. 15 at 357.

parties to the contract from which the dispute has arisen. Exceptionally, this may differ from the national law governing the interpretation of the agreement to submit the dispute to arbitration. Less exceptionally it may also differ from the national law which the parties have expressly or by implication selected to govern the relationship between themselves and the arbitrator in the conduct of the arbitration: the 'curial law' of the arbitration as it is often called.

Toulson J read the words 'less exceptionally it may also differ' as meaning 'the substantive law governing the contract and the law governing the arbitration agreement are more likely to differ where there is a different choice of procedural law', and from that proceeded to the conclusion that they are *likely* to differ where there is a different procedural law. But this is not what Lord Mustill says; quite the reverse. What he says is that it is more unlikely that there will be a difference between the law applicable to the arbitration agreement and the law applicable to the substance of the dispute than that there will be a difference between the law applicable to the substance of the dispute and the law applicable to the arbitral procedure. In other words, Lord Mustill in *Channel Tunnel* advocated precisely the opposite approach to Toulson J's in *XL v. Owens Corning*. He considered that the law applicable to the substance of the contract exercised a stronger gravitational attraction over the validity and interpretation of the arbitration agreement than did the procedural law.¹⁸ This is, at all events, the view of most commentators.¹⁹ It also seems logical. Even if juridically separable, the arbitration agreement forms part of a single document, and if the parties have expressly chosen a law to govern the obligations therein, there is no obvious reason not to regard that choice as extending to *all* the obligations, including the obligation to arbitrate. The arbitration agreement is an 'agreement inside an agreement',²⁰ not an agreement alongside an agreement.

Toulson J's reliance upon the express reference to the English Arbitration Act 1996 is also questionable. With two exceptions,²¹ that Act has nothing to say about the contractual validity of arbitration agreements as such. It is about procedure. Therefore the parties' express reference to the Arbitration Act 1996 is highly unlikely to have reflected any intention concerning the law that would govern the validity or interpretation of the arbitration agreement. It does indicate

¹⁸ But see Mustill J's comments in *Black Clawson International Ltd v. Papierwerk Waldhof-Aschaffenburg AG* [1981] 2 Lloyd's Rep. 446, 453, which appear to suggest that the law governing the agreement to arbitrate is likely to be the same as the '*lex fori*'.

¹⁹ For: Dicey and Morris, *supra* n. 5 at vol. 1, p. 597; A. Redfern and M. Hunter, *International Commercial Arbitration* (3rd edn., Sweet & Maxwell, London, 1999), p. 158; Restatement (Second) of Conflict of Laws, § 218, comment d. Against: R. Plender and M. Wilderspin, *The European Contracts Convention* (Sweet & Maxwell, London, 2001), p. 70; Gary B. Born, *International Commercial Arbitration* (2nd edn., Kluwer Law International, The Hague, 2001), p. 210.

²⁰ *Union of India v. McDonnell Douglas Corp.* [1993] 2 Lloyd's Rep. 48, 49–50 (express choice of Indian law to govern the contract, but arbitration in London: held that arbitration agreement was governed by Indian law but procedure by English law).

²¹ The two exceptions are found in ss. 7 and 8 of the 1996 Act. Section 7 expressly enacts the separability doctrine. Section 8 prevents the discharge of an arbitration agreement by the death of a party. A provision reversing that common law rule was first enacted in the Arbitration Act 1934.

an intention that English law should apply *procedurally*.²² But that adds nothing to Toulson J's first point; and if he is wrong in his approach to the significance of the procedural law over the substantive applicable law, the parties' express reference to the 1996 Act will not rescue his conclusion.

If one were writing on a blank slate, there might be much to be said for Toulson J's approach. Once the separability of the arbitration agreement is wholeheartedly embraced, there is much to be said for the view that a choice of law directed primarily at the resolution of substantive disputes should not be assumed to apply to the rather different question whether a dispute resolution agreement is valid. Where the law applicable to the substance of the dispute and to the procedure for the resolution of the dispute differ,²³ it may well make sense that the procedural law should also govern the validity and interpretation of the agreement to arbitrate. It may fairly be objected that this is an illogical approach; but it seems no more inherently illogical than other consequences of the separability doctrine, whose justification is essentially pragmatic. Thus, while the reasoning in Toulson J's decision in *XL v. Owens Corning* is hard to support, and the result seems inconsistent with such authority as exists (including the *dicta* of Lord Mustill in *Channel Tunnel*), it may be thought pragmatically to reach a sensible result.

II. THE INTERNAL PROCEDURAL LAW OF THE ARBITRATION

There is no doubt that the internal procedural law and rules of any arbitration under the Bermuda Form are those found in the English Arbitration Act 1996. These are expressly referred to in the Bermuda Form (either directly or, in early versions of the Form, by reference to any statutory 'modifications or amendments' of the Arbitration Acts 1950, 1975 and 1979). In any case, the Act is of mandatory application to any arbitration whose 'seat' is in England,²⁴ and the English courts have supervisory powers to ensure that it is applied.

The statutory rules governing the conduct of arbitration proceedings under the Arbitration Act 1996 are found in sections 33 to 41 of the Act. They give a very considerable amount of leeway to the parties and the tribunal. There is a minimal framework of mandatory provisions.²⁵ The tribunal must 'act fairly and impartially' and 'adopt procedures suitable to the circumstances of the case, avoiding unnecessary delay and expense, so as to provide a fair means for the

²² Recent versions of the Bermuda Form expressly apply the law of England 'as respects arbitration *procedure*' (emphasis added).

²³ Compare the Restatement (Second) of Conflict of Laws, § 218, which assumes that a choice of law for the contract will probably extend to the arbitration agreement (comment b) but also that the law governing the arbitration *agreement* will also govern arbitral procedure (comment d).

²⁴ Arbitration Act 1996, ss. 2(1), 3. But it is not necessary that all the hearings and deliberations of the tribunal should take place in England. The tribunal may decide to hold hearings at any convenient location without thereby varying the 'seat'.

²⁵ English Arbitration Act 1996, s. 4(1) and Sch. 1.

resolution of the matters falling to be determined'.²⁶ The parties must co-operate by doing 'all things necessary for the proper and expeditious conduct of the arbitral proceedings' including complying 'without delay' with any procedural directions given by the tribunal.²⁷ These leave a wide field within which the parties and the tribunal are largely²⁸ free to shape the arbitral procedure as they think fit. The Act provides various default powers and rules, but these should be modified to meet the particular circumstances of the dispute.

A central provision is section 34(1), which gives the tribunal power to decide 'all procedural and evidential matters'. That expressly includes matters such as whether there should be pleadings, whether documents should be disclosed (and if so on what basis), whether the strict rules of evidence should be applied, and how submissions should be made.²⁹ There is therefore no requirement that the tribunal should follow the procedures or practices that would be applied in an English court, and as a practical matter the procedures adopted are normally different in various respects. For instance, an English court would require any question of foreign law (including New York law) to be 'proved' as a matter of fact by calling expert witnesses who would be examined and cross-examined.³⁰ Although an arbitration tribunal could in theory follow this procedure, the invariable modern practice in arbitrations under the Bermuda Form is to deal with New York law by way of submission, rather than to hear 'evidence' on it.³¹

This article does not consider the practical aspects of the conduct of a Bermuda Form arbitration.³² The distinction between issues of 'procedure' (governed by English law) and issues of 'substance' (governed by New York law) is, however, discussed in more detail below.³³

III. CURIAL LAW: JUDICIAL SUPERVISION OF THE ARBITRAL PROCESS

Because the juridical seat of the arbitration is in England,³⁴ it will be subject to the supervisory jurisdiction of the English High Court under the English Arbitration Act 1996.³⁵ The English court would, if necessary, exercise its powers

²⁶ *ibid.* s. 33.

²⁷ *ibid.* s. 40.

²⁸ There are a few other mandatory provisions of the Act relevant to procedure during the course of a reference, involving what constitutes an expense of the arbitration (s. 37(2)), the availability of compulsory process to secure the attendance of witnesses (s. 43), the power to withhold an award if the tribunal's fees have not been paid (s. 56) and the award of costs (s. 60).

²⁹ Arbitration Act 1996, s. 34(2). The list is not exhaustive.

³⁰ See Dicey and Morris, *supra* n. 5 at ch. 9.

³¹ For judicial recognition of this practice, see *Reliance Industries Ltd v. Enron Oil and Gas India Ltd* [2002] 1 Lloyd's Rep. 645, at 649 n. 8.

³² This topic is covered in a number of chapters of *Liability Insurance in International Arbitration: The Bermuda Form*, *supra* n. *. For a general description, including cultural differences that might surprise US attorneys arbitrating in London, see Dasteel and Jacobs, 'American Werewolves in London' in (2002) 18(2) *Arbitration International* 165.

³³ See *infra*.

³⁴ See *supra*.

³⁵ Arbitration Act 1996, s. 2(1).

to appoint or remove arbitrators.³⁶ It would deal with any issue as to the tribunal's jurisdiction,³⁷ and with any complaint of serious procedural irregularity in the course of the hearing.³⁸ The most famous peculiarity of the English supervisory jurisdiction – the possibility of an appeal to the court on a point of law³⁹ – will not arise: in the first place because it is expressly excluded by agreement,⁴⁰ and in the second place because 'New York law' would be regarded, for these purposes, as fact rather than law.⁴¹

IV. LAW GOVERNING CHOICE OF LAW

The choice of law rules applicable to a given dispute are normally regarded as a matter for the law of the forum.⁴² In the context of an international arbitration taking place in England, and governed by the Arbitration Act 1996, the starting point is the Act itself, which contains an express provision for international arbitrations, different (in some respects) from the rules that would be applied by an English court.⁴³ For present purposes, two provisions matter. First, under section 46(1) the tribunal is directed to apply the law chosen by the parties. One need not, under the Bermuda Form, look any further, therefore, than the express choice of New York law. Secondly, under section 44, the Act permits the parties to opt for a decision to be made according to *non-legal* principles, should they wish to do so. That is significant, in this context, because it removes any lingering doubt about the permissibility of adopting a 'pick-and-mix' approach to choice of law, whereby the parties do not simply choose a system of law, but adopt that system with modifications, by providing for disputes to be determined 'in accordance with such other considerations as are agreed'.

Since, strictly, it is English legal rules, and specifically the statutory choice of law rules applicable to arbitrations,⁴⁴ that govern the choice of law question, the interpretation and validity of the choice of law provisions are matters for English law, not New York law. New York choice of law rules, in particular, are irrelevant.

³⁶ *ibid.* ss. 18–19 (appointment), 24 (removal).

³⁷ *ibid.* ss. 32, 67. Section 37 enables an application to be made, with the consent of the parties or the tribunal's position, in the course of the reference. Section 67 relates to challenges to an award on the ground that it was made without jurisdiction.

³⁸ *ibid.* s. 68.

³⁹ *ibid.* s. 69.

⁴⁰ *ibid.* s. 69(1): 'Unless otherwise agreed by the parties ...' an appeal lies.

⁴¹ *ibid.* s. 82(1); *Egmatra AG v. Marco Trading Corp.* [1999] 1 Lloyd's Rep. 862, at 865; *Sanghi Polyesters Ltd (India) v. The International Investor (KCFC) Kuwait* [2000] 1 Lloyd's Rep. 480, at 483. Where the parties prefer to proceed on the basis that the chosen foreign law is the same as English law (but without agreeing to vary the applicable law), the resulting decision is not a decision of 'law' for the purposes of an appeal: *Reliance Industries Ltd v. Enron Oil and Gas India Ltd* [2002] 1 Lloyd's Rep. 645.

⁴² Subject to *renvoi*, which does not apply in contract cases. See *infra* n. 50.

⁴³ Contracts (Applicable Law) Act 1990, enacting the Rome Convention on the Law Applicable to Contractual Obligations. That Act too requires the court to give effect to an express choice of law, but it might be an open question whether it permits the parties to modify that law in particular respects, as the Bermuda Form purports to do.

⁴⁴ The question might, in theory, arise whether those provisions should be given effect if English law (giving effect to European Community law) restricted the parties' choice of law, as it sometimes does.

As a matter of basic principle, a choice of contractual governing law is taken as not including the choice of law rules of the selected legal system:⁴⁵ the doctrine of *renvoi* is not applied to contracts.⁴⁶ That position is placed beyond any doubt by the express reference to the ‘internal’ law of New York, which excludes recourse to New York’s private international law.⁴⁷

V. APPLICABLE SUBSTANTIVE LAW

a. *The Basic Choice*

By express choice, the contract is governed by the ‘internal laws of the State of New York’ subject to certain modifications. Why the reference to New York’s ‘internal’ law? There are two possibilities. The first is that it evinces an intention that New York *state* law should apply, but that US *federal* law, although applicable in New York, does not. This seems improbable, because it is hard to see that the drafters of an insurance policy should anticipate that federal law would have any significant impact anyway.⁴⁸ And if, by chance, it did, it would likely be very hard to disentangle federal law, so as to identify the substratum of state law below the surface. It therefore seems more likely that the reference to the ‘internal’ law of the state of New York is intended to make it clear that New York’s private international law rules are not to be applied.⁴⁹

English law regards issues of initial validity, and allied questions such as the effect of misrepresentation or duress upon a contract, as matters governed by the ‘putative’ applicable law; that is, the law that would be applicable assuming a contract had been made. This now has statutory warrant for cases in court,⁵⁰ reflecting what appears to have been the position at common law.⁵¹ Where the Arbitration Act refers⁵² to the law chosen by the parties being used to determine

⁴⁵ Arbitration Act 1996, s. 46(2).

⁴⁶ See *infra* n. 50.

⁴⁷ See *further infra*.

⁴⁸ Insurance law is largely a subset of general contract law, and thus a matter of state rather than federal law, in the USA. See *e.g.* *Zurich Ins Co. v. Shearson Lehman Hutton, Inc.*, 618 N.Y.S. 2d 609, 613 (1994). There are exceptions, such as employee benefit plans which generally are subject to the Employee Retirement Income Security Act (ERISA), 29 USC §§ 1001 *et seq.*, a federal statute to which federal common law principles of interpretation apply under the doctrine of pre-emption. But that is not likely to affect issues relating to the Bermuda Form.

⁴⁹ This is consistent with the general approach taken to choice of law in contract: see *e.g.* *Amin Rasheed Shipping Corp. v. Kuwait Ins. Co.* [1984] AC 50, at 61–62; Contracts (Applicable Law) Act 1990, Sch., para. 15; Restatement (Second) of Conflict of Laws, § 187(4). It might therefore be objected that expressly spelling it out in the policy would be surplusage: but arguments about surplusage are always weak in commercial contracts, since drafters ‘frequently use many words ... out of a sense of caution’ (*Norwich Union Life Ins. Soc. v. British Railways Board* (1987) 283 EG 846). It is by no means unprecedented, in our experience, to find an express exclusion of *renvoi* in a contractual choice of law provision.

⁵⁰ Rome Convention, Art. 8; Contracts (Applicable Law) Act 1990, Sch.

⁵¹ *Re Bonacina* [1912] 2 Ch. 394 (consideration), *Mackender v. Feldia* [1966] 3 All ER 847, *Evans Marshall v. Bertola* [1973] 1 All ER 992.

⁵² Arbitration Act 1996, s. 46.

‘the dispute’, it therefore includes within the ambit of the ‘dispute’ a dispute about the validity of the contract. This, too, will therefore be governed by New York law.⁵³

b. Exclusion of Insurance Regulatory Law

Recent versions of the Bermuda Form exclude New York law in so far as it ‘pertains to regulation under the New York Insurance Law’ or to ‘regulations’ issued by the Insurance Department of the State of New York applying to insurers doing business in the state. The focus is exclusively on *regulatory* statutes. It would not, for instance, be open to the parties to rely on some breach of New York regulatory law to invalidate the policy. It does not exclude those parts of the New York Insurance Law which state or amend the law governing the civil rights and obligations of insurers and policyholders between themselves. For instance, it does not stand in the way of the application of those parts of the New York Insurance Law which deal with the effect of misrepresentation and non-disclosure, or the effect of a breach of warranty.

c. Modification of New York Law: Punitive Damages

Under New York law, punitive damages⁵⁴ are not insurable, as a matter of public policy.⁵⁵ As a matter of construction, the parties to the Bermuda Form clearly intended punitive damages to be recoverable under the policy. It might well be that a New York court would decline to apply a choice of law provision which attempted to circumvent this policy, just as it would decline to enforce the policy’s extension of punitive damages. In addition, the punitive damages for which insurance is sought may have been awarded under the law of a state other than New York; in such instances, some courts have found under New York law that this issue is governed by the law of the state making the award of punitive damages.⁵⁶ But since English law governs the validity of the choice of law provision, that does not matter. In *Lancashire County Council v. Municipal Mutual Insurance Ltd*,⁵⁷ the Court of Appeal held that English law does not prohibit insurance of liability for punitive damages, even where the punitive damages are awarded by an English court. There might be difficulty if the insurance policy sought to provide indemnity where the policyholder was found to have

⁵³ In US private international law, an *expressly* chosen law is not necessarily applied to such issues. But that does not matter, since it is English not New York law that governs choice of law issues.

⁵⁴ Usually known in English law as ‘exemplary’ damages.

⁵⁵ *Soto v. State Farm Ins. Co.*, 613 N.Y.S. 2d 352 (1994); *Hartford Accident & Indem. Co. v. Village of Hempstead*, 422 N.Y.S. 2d 47 (1979); *Town of Massena v. Healthcare Underwriters Mut. Ins. Co.*, 724 N.Y.S. 2d 102 (3d Dept 2001); *cf. Zurich Ins. Co. v. Shearson Lehman Hutton, Inc.* 618 N.Y.S. 2d 609 (1994); *Home Ins. Co. v. American Home Products Corp.* 551 N.Y.S. 2d 481 (1990). See also Eugene R. Anderson, Jordan S. Stanzler and Lorelie S. Masters, *Insurance Coverage Litigation* (2nd edn., Aspen, 2001), ch. 8.

⁵⁶ See e.g. *Hoechst Celanese Corp. v. National Union Fire Ins. Co. of Pittsburgh, Pa.*, 1994 Del. Super. Lexis (22 April 1994). See also Anderson, Stanzler and Masters, *supra* n. 55 at § 8.

⁵⁷ [1997] QB 897.

committed a crime,⁵⁸ but that is unlikely to be an issue in the sort of case with which the Bermuda Form is concerned. *Lancashire County Council v. Municipal Mutual* was directed at a case where the liability to pay punitive damages was vicarious, and formally leaves open the question whether a tortfeasor whose personal conduct was opprobrious could recover. However, liability normally will be vicarious where a claim is made by a company under the Bermuda Form, and there seems little reason why a policyholder who otherwise meets the requirements for coverage (including the absence of any intention to cause injury) should not be indemnified.

An arbitration tribunal is not therefore precluded from giving effect to the clear intention of the parties that the Bermuda Form should be available to respond to losses caused by awards of punitive damages. Applying English law, and English public policy, to the choice of law provision, the New York law policy that would deny recovery in such cases can be disregarded. If it were ever necessary to seek judicial enforcement of an award giving indemnity for punitive damages in a jurisdiction – whether New York or elsewhere – which regards such liability as uninsurable, problems might arise. But fortunately judicial enforcement of arbitration awards under the Bermuda Form is rarely necessary, and even if necessary the enforcement would be unlikely to take place in New York.

d. Modification of the Canons of Construction: Validity

As noted above, the choice of law provision seeks to spell out an approach to interpretation that differs, in various ways, from the approach ordinarily taken by the New York courts when interpreting insurance contracts:

[T]he provisions, stipulations, exclusions and conditions of this Policy are to be construed in an evenhanded fashion as between the Insured and the Company; without limitation, where the language of this Policy is deemed to be ambiguous or otherwise unclear, the issue shall be resolved in the manner most consistent with the relevant provisions, exclusions and conditions (without regard to authorship of language, without any presumption or arbitrary interpretation or construction in favor of either the Insured or the Company [or reference to the ‘reasonable expectations’ of either thereof or to *contra proferentem*]⁵⁹ and without reference to parol [or other extrinsic]⁶⁰ evidence)

Later versions of the Bermuda Form add ‘without reference to the reasonable expectations of either of the parties’ and extend to ‘extrinsic’ as well as ‘parol’ evidence.

If this clause came before a New York court the question might arise as to the extent to which the modification of New York law principles of contract interpretation was valid in the light of New York public policy. For example, would a policy term purporting to preclude the use of parol or extrinsic evidence

⁵⁸ *ibid.* at 907; *Gray v. Barr* [1971] 2 QB 554 (‘deliberate, intentional and unlawful violence’).

⁵⁹ These words do not appear in the original versions of the Form.

⁶⁰ These words do not appear in the original versions of the Form.

be void as against public policy?⁶¹ How would a New York court react to the clause in the light of the principle that a literal construction of the policy language is not appropriate if such a construction thwarts the clear purpose of the contract or leads to an absurd result?⁶² Is it permissible for an insurance company drafter to oust the ordinary *contra proferentem* rule, which is a rule rooted in fairness?

However, all this is irrelevant where the arbitration is taking place in England, for English law makes it quite clear that the parties are free to agree to whatever rules they wish governing the contract.⁶³ And English law would certainly not regard any of the modifications to the canons of construction as offensive to English public policy. In practice, arbitration tribunals in Bermuda Form arbitrations apply modified New York law as provided for in the clause.

VI. LAW GOVERNING THE UNDERLYING CLAIM

Since the Bermuda Form is a liability policy, a claim under it always rests upon some legal claim brought against the policyholder by third parties. As a result, it sometimes becomes necessary to consider legal systems other than England and New York, as part of the factual background of the case. For example, a policyholder who is seeking to establish that a particular settlement was 'reasonable' may need to explain why there was a perceived risk of liability under the state law applicable to the settled claim.

⁶¹ In the light of our conclusion *supra*, we do not address this issue in the detail which it might otherwise deserve. The general principle is that contract terms freely negotiated are valid unless they violate New York public policy. In *Slayko v. Security Mutual Insurance Co.*, 98 N.Y. 2d 289 (2002), the New York Court of Appeals upheld a clause in a homeowners' policy excluding liability for criminal activity, and said that 'when statutes and Insurance Department regulations are silent, we are reluctant to inhibit freedom of contract by finding insurance policy clauses violative of public policy'. See also *Joseph R. Loring and Assocs Inc. v. Continental Casualty Co.*, 56 N.Y. 2d 848, 453 N.Y.S. 2d 169 (1982) where the Court of Appeals held that a claims made policy did not violate public policy. See too the authorities which indicate that parties can waive rules of evidence or in other ways make the law that will bind them: *Brady v. Nally* 151 N.Y. 258, 264–265 (1896); *Mitchell v. New York Hospital* 61 N.Y. 2d 208, 214; 473 N.Y.S.2d 148, 151 (1984); *Martin v. City of Cohoes* 37 N.Y.2d 162, 371 N.Y.S.2d 687, 690 (1975); *In re Malloy's Estate* 278 N.Y. 429, 433 (1938). In *HRH Construction Corp. v. Bethlehem Steel Corp.* 45 N.Y.2d 675, 682, 412 N.Y.S. 2d 366, 369 (1978), the court held that it was open to parties to agree the 'substantive rule on the basis of which the award was to be made in their arbitration proceedings' provided that it did not 'run afoul of public policy'. If the Bermuda Form modification of New York law was to be challenged on the grounds of violation of New York public policy, questions might arise as to whether New York public policy applied in the context of a high-level excess cover between an assured and insurer neither of whom might be domiciled in New York, and who had agreed to submit their disputes to London arbitration. For authorities which could perhaps be relied upon in support of a challenge, see *Cronk v. State of New York*, Court of Claims 100 Misc. 2d 680, 420 N.Y.S. 2d 113 (1979) (clause pre-empting the court from considering legally competent evidence held to void as against public policy), and *Allstate Insurance Co. v. White Metal Rolling & Stamping Corp.* 466 F. Supp 419 (E.D.N.Y. 1979) ('entire agreement' clause did not preclude extrinsic evidence of declarations of intention to resolve an ambiguity or equivocation). See also Lorelie S. Masters, 'Arbitration Clauses in Liability Policies: A Ticket to Ride' in (1996) 9(4) *John Liner Rev.* 33; Dolin and Posner, *supra* n. 1 at pp. 76–77.

⁶² *McGrail v. Equitable Life Assur. Soc'y of the US*, 55 N.E. 2d 483 (1944); *Evanston Ins. Co. v. GAB Bus Serv.*, App Div 521 N.Y.S. 2d 692 (1987).

⁶³ Arbitration Act 1996, s. 46. See *supra*. The last sentence of the XL 004 form appears to be directed at the possible argument based on New York public policy, by providing that the 'internal laws of England and Wales' apply to 'the extent that New York law is inapplicable by virtue of any exception or proviso enumerated above'.

Where this issue arises, however, it is only ever as a matter of factual background. Under English law it may be necessary, depending upon the wording of the liability insurance policy, for the policyholder to prove that there *was* a liability. Where a case is settled, it is not enough to show that the policyholder faced a risk that a particular court or a particular jury would or might have reached an adverse verdict: the anticipated verdict must be shown to be, in some objective sense, ‘right’ as a matter of law.⁶⁴ This approach, which rests on a questionable jurisprudential premise,⁶⁵ the product of a rarefied legal consciousness divorced from the practical realities of life before juries in US state courts, is totally foreign to New York’s approach to this question as it arises under liability policies.⁶⁶ The law applicable to the underlying cases is relevant only for the light it throws, which may sometimes be oblique, on the practical risks that the policyholder faced in litigation. As such, it might sometimes be helpful for a tribunal, which typically includes members who have no practical experience in civil jury litigation, to be instructed on such issues by means of expert evidence. This expert evidence can help place the legal principles in a practical context, and take them out of the purely theoretical context that might exist were the tribunal simply to hear submissions on such questions. But each case varies, and the tribunal should adopt whatever procedure seems best fitted to the circumstances.

VII. THE DIVISION BETWEEN SUBSTANCE AND PROCEDURE

Since procedural questions are governed by English law, in the form of the English Arbitration Act 1996, while substantive questions are governed by New York law, it can sometimes matter whether a particular issue is treated as substantive or procedural.⁶⁷ Since that question arises as part of the choice of law process, it is a matter of English law.

⁶⁴ *Skandia International Corp. v. NRG Victory Reinsurance Ltd* [1998] Lloyd’s Rep. IR 439; *MDIS v. Swinbank* [1999] Lloyd’s Rep. IR 516; *Thornton Springer v. NEM Ins. Co. Ltd* [2000] Lloyd’s Rep. IR 590; *Structural Polymer Systems v. Brown* [2000] Lloyd’s Rep. IR 64, at 68.

⁶⁵ It assumes that there is a ‘right legal answer’ to any case divorced from the result the institutions of the system would actually generate. *cf.* Justice Holmes: ‘Take the fundamental question, what constitutes the law? ... The prophecies of what the courts will do in fact, and nothing more pretentious, are what I mean by the law’: ‘The Path of the Law’ in (1897) 10 *Harvard Law Review* 457.

⁶⁶ *See e.g.* the decision in *Luria Brothers & Co. v. Alliance Assurance Co. Ltd* 780 F. 2d 1082 (2nd Cir. 1986): ‘In order to recover the amount of the settlement from the insurer, the insured need not establish actual liability to the party with whom it has settled so long as a potential liability on the facts known to the [insured is] shown to exist, culminating in a settlement in an amount reasonable in view of the size of possible recovery and degree of probability of claimant’s success against the [insured]’. *See also Uniroyal Inc. v. Home Ins. Co.* 707 F. Supp. 1368, 1378 (E.D.N.Y. 1988), and Anderson, Stanzler and Masters, *supra* n. 55.

⁶⁷ The distinction between substance and procedure remains part of the orthodox English approach to the conflict of laws: *see* Dicey and Morris, *supra* n. 5 at vol. 1, p. 157 (Rule 17). In the USA, the Restatement (Second) of Conflict of Laws abandoned reliance upon the classification of rules as ‘substance’ or ‘procedure’ because it was thought to produce crude decision-making: § 122, comment (b). As will become apparent, modern English practice makes finer distinctions than a straightforward division by reference to ‘substance’ and ‘procedure’ might suggest.

a. Burden of Proof

At common law there was some doubt whether issues of burden of proof were procedural or substantive.⁶⁸ In court proceedings in England concerning contracts, the question is now resolved by statute. The law applicable to the contract applies ‘to the extent that it contains, in the law of contract, rules which raise presumptions of law or determine the burden of proof’.⁶⁹ It is for English law to decide whether a rule about burden of proof should be regarded as part of the law of contract (in which case it is governed by the applicable law), or part of the foreign legal system’s general legal rules (in which case it is not).⁷⁰ This statutory rule does not formally apply in arbitration, but the tribunal is free to decide to apply it.⁷¹ Since this statutory rule may reflect the common law⁷² and is consistent with the views of most commentators, it is suggested that the same approach would be taken. For most practical purposes, New York rules relating to the burden of proof will be applied, since these rules are part of the relevant law of contract. So a tribunal will apply New York law in determining whether a particular provision is to be treated as an exclusion from coverage (where the burden lies on the insurer) or part of the primary definition of coverage (where it lies on the policyholder). And it will apply New York law whereby the burden of proving material misrepresentation lies on the insurer.⁷³

b. Interpretation

It is unfortunate that rules of contractual interpretation sometimes masquerade as evidential rules: it is said that a particular line of argument is barred by the ‘parol evidence rule’ or that particular material offered to assist in interpretation is ‘inadmissible’ for that purpose. It is well established that, despite this terminology, the relevant rules are rules of substance not procedure.⁷⁴ What facts are relevant to interpretation is determined by the applicable law (or such other rules as the parties have, as the Arbitration Act 1996 permits, selected). Insofar as any question of ‘admissibility’ arises, it arises because evidence that is irrelevant should not be considered. To adopt any different classification would, as Dicey and Morris

⁶⁸ There is authority that the burden of proof is a procedural issue: *The Roberta* (1937) 58 Ll L R 159 at 177, *In re the Estate of Fuld (No. 3)* [1968] P 675 at 696–97. But Dicey and Morris, citing certain comments of Lorenzen with approval, consider that there is ‘much to be said for treating them as substantive’, at least where their effect is to shape substantive rights: Dicey and Morris, *supra* n. 5 at vol. 1, p. 167.

⁶⁹ Contracts (Applicable Law) Act 1990, Sch., para. 14.

⁷⁰ See C. G. J. Morse, ‘The EEC Convention on the Law Applicable to Contractual Obligations’ (1982) 2 *YEL* 107, at p. 156; Richard Plender and Michael Wilderspin, *The European Contracts Convention* (Sweet & Maxwell, London, 2001), paras 10–13, 10–14.

⁷¹ Either directly under s. 46 (as a choice of law rule) or indirectly under s. 34 as a procedural rule.

⁷² See *supra* n. 69.

⁷³ See e.g. *First Fin. Ins. Co. v. Allstate Interior Demolition Corp.* 193 F. 3d 109 (2d Cir. 1999) (applying New York law).

⁷⁴ *St Pierre v. South American Stores Ltd* [1937] 3 All ER 349 at 351, *AB Bofors v. AB Skandia* [1982] 1 Lloyd’s Rep. 410 at 412, *Amin Rasheed Corp. v. Kuwait Ins.* [1984] AC 50. But the contrary decision in *Körner v. Witkowitz* [1950] 2 KB 128, aff’d as *Vitkovic v. Körner* [1951] AC 869, is problematic, and the explanation offered of it by Dicey and Morris, *supra* n. 5, is not altogether convincing, since it appears to beg the question, and to have no obvious rational basis.

points out, 'be tantamount to distorting the foreign law'.⁷⁵ Thus, it is New York law, as modified by the parties, that governs such questions.

c. Estoppel

In English law, estoppels are sometimes said to be rules 'of evidence'. But it seems clear that they are not 'ordinary' rules of evidence. They often arise out of, or affect, or define, substantive rights: 'It is true that estoppels can be described as rules of evidence or as rules of public policy to stop the abuse of process by relitigation. But that is to look at how estoppels are given effect to, not at what is the nature of the private law right which the estoppel recognises and protects'.⁷⁶ Although there is authority for the proposition that estoppel is an issue for the *lex fori* (i.e. the law of the court hearing the matter), it is not unequivocal even in the context of estoppel *per rem judicatam*.⁷⁷ It may be that some estoppels are properly regarded as substantive, some as procedural.⁷⁸ Nor is it clear whether, if 'procedural', the discretion given to tribunals as to the procedures to be followed in arbitration extend to the question whether an estoppel should be recognized in particular circumstances. In *Ali Shipping Corporation v. Shipyard Trogir*⁷⁹ the Court of Appeal assumed that English law, including the rule requiring identity of the parties to found an issue estoppel, would apply to determine whether an estoppel was created by an earlier arbitration award. But it was not explained whether this was because English law was the procedural law of the arbitration, or because English law applied to the substance of the claim; and it does not appear to have been argued that any other principle could be applied.

Whatever the position with regard to estoppel, principles of waiver, election and affirmation are certainly regarded as substantive principles of law, since they are so intimately linked with substantive rights. And, whether procedural or substantive, decisions about estoppel are for the arbitrators.⁸⁰

d. Limitation

The classification of rules governing the limitation of actions has been notoriously problematic. The traditional English common law approach has been to treat (most) English limitation periods as procedural, but to recognize the possibility that a foreign limitation period might be substantive, depending on whether it was interpreted as barring 'the right' or 'the remedy'. This led to considerable

⁷⁵ Dicey and Morris, *supra* n. 5 at vol. II, p. 1262.

⁷⁶ *Associated Electric and Gas Insurance Services Ltd v. European Reinsurance Co. of Zurich* [2003] 1 WLR 1041, at para. 15 (Lord Hobhouse).

⁷⁷ *Carl Zeiss Stiftung v. Rayner & Keeler Ltd (No. 2)* [1967] 1 AC 853 at 919, per Lord Reid: 'It is quite true that estoppel is a matter for the *lex fori* but the *lex fori* ought to be developed in a manner consistent with good sense'. The principle of estoppel *per rem judicatam* applies where there has been a previous court decision (a *res judicata*) on a matter.

⁷⁸ See Dicey and Morris, *supra* n. 5 at vol. 1, p. 168.

⁷⁹ [1999] 1 WLR 314.

⁸⁰ *Associated Electric and Gas Insurance Services Ltd v. European Reinsurance Co. of Zurich* [2003] 1 WLR 1041.

complexity, and to problems of so-called ‘cumulation’ and ‘gap’. However, under the Foreign Limitation Periods Act 1984, limitation is now generally treated as a substantive question, subject to the *lex causae*.⁸¹ This approach is, under the English Arbitration Act 1996, applied in arbitration.⁸² Thus, in a case under the Bermuda Form, the relevant limitation period is the six-year period laid down by New York law.

e. Remedies

Remedies are tricky; they cannot be neatly categorized as matters of substance or of procedure. A distinction is customarily drawn between claims for damages and other remedies.

The question of what sorts of damage are compensable was at common law regarded as a matter for the *lex causae*.⁸³ Questions about the precise proof and quantification of damages were then again a matter for the *lex fori*: one was back in the realm of procedure and evidence. In contractual cases before English courts, there is now a statutory rule that damages, in so far as they are subject to legal rules, are a matter for the applicable law,⁸⁴ but always within the ‘limits’ of the court’s procedural powers. Moreover, the applicable law governs only the ‘consequences of breach, including assessment of damages *in so far as it is governed by rules of law*’, which seems to leave open the application of the *lex fori* to issues about how detailed facts should be proved. It is hard to see any material difference between this and the common law position. In an arbitration, the tribunal will be entitled to use its procedural discretion to decide how questions of ‘detailed proof’ or ‘assessment’ should be approached.

Other remedies are more controversial. Obviously, the English Arbitration Act 1996 governs to the extent that it places statutory limits on the type of remedy the tribunal may order. But that is not a practical difficulty, since the range of available options is wide. Where there may be room for debate is upon the issue whether, in a particular case, a given remedy should be deployed – and if so on what terms. Suppose that New York law permits an insurer to rescind a contract for misrepresentation without returning the premium, as is sometimes (though in our view wrongly) suggested. Should an arbitration tribunal pursue that course, or should it permit rescission only on terms which require return of the premium, as English law does? Or suppose that the insurer seeks a ‘negative declaration’ that it will not be liable if certain events take place, for instance if the attachment point is exceeded in the future. Should the tribunal apply the English approach to deciding when such negative declarations are appropriate, or should it be guided by the circumstances in which such relief would be granted in New York?

⁸¹ See also Contracts (Applicable Law) Act 1990, Sch., para. 10(1)(d) (prescription and limitation governed by the applicable law of the contract).

⁸² Arbitration Act 1996, s. 13(1), (4).

⁸³ *Boys v. Chaplin* [1971] AC 356 at 379, 393, 394–395.

⁸⁴ Contracts (Applicable Law) Act 1990, Sch., para. 10(1)(c).

The traditional English view is that choice between remedies is dictated by the principles customarily applied by the forum. On this theory an English court or tribunal may order specific performance of a contract in circumstances where the *lex causae* would not, or restrict the claimant to damages in circumstances where the *lex causae* would grant specific performance, and so on.⁸⁵ But even in court, there are limits: the remedy granted must not be such as to alter fundamentally the nature and scope of the right as it is conceived under the *lex causae*.⁸⁶ In litigation, the Contracts (Applicable Law) Act 1990 seems to go rather further, since it mandates that (within the limits of the powers conferred upon the court deciding the case)⁸⁷ ‘the consequences of breach’ are governed by the applicable law.

Although the statute does not apply directly or automatically in an arbitration, there seems to be good reason why an international arbitration tribunal should generally prefer to produce an award which is as close as possible to that which the applicable law chosen by the parties would arrive at. Arbitral seats are selected largely for their neutrality; their awards may well not even be enforced or performed at the seat. Even if the granting or withholding of the normal remedy which would be available under the chosen law does not totally pervert the right, it is not unlikely to change it quite significantly. If it were the case that New York law permitted an insurer to rescind a policy yet retain the premium, an order requiring the return of the premium as the price of rescission would unjustifiably alter the parties’ rights.

Negative declarations are trickier. The restrictions on the grant of such declarations do not derive from any particular conception of *rights* under the contract, or even the juridical ‘consequence of breach’, but from variable conceptions of the proper role of a judicial body, often with constitutional overtones. The qualms a court in New York may feel about granting such declarations do not obviously carry over to a private tribunal sitting in England. Nor, indeed, do the qualms that an English court may feel.⁸⁸ As public tribunals, courts have to juggle various policy considerations which may militate in favour of a fairly restrictive approach to ‘hypothetical’ or ‘advisory’ remedies. They must consider their constitutional role compared to that of the legislature, the proper use of publicly funded court time, and the suitability of a rather inflexible and formal procedure for deciding such questions. Arbitration tribunals do not work within the same constraints: they are privately funded, constitutionally uninfluential, and capable of moulding their procedure more flexibly than a court can. There are aspects of granting relief in relation to disputes that may be hypothetical they should worry about, such as the cost and expense for an

⁸⁵ *Baschet v. London Illustrated Standard Co.* [1900] 1 Ch. 73. See generally Dicey and Morris, *supra* n. 5 at vol. 1, p. 159.

⁸⁶ *Phrantzes v. Argenti* [1960] 2 QB 19 at 35.

⁸⁷ A court could not use the *lex causae* to acquire a remedial power it lacks, but only to choose between the exercise of its various remedial powers.

⁸⁸ Or, perhaps, used to feel: English courts now regard negative declarations with more fortitude than previously: see e.g. *Messier Dowty Ltd v. Sabena S.A.* [2000] 1 Lloyd’s Rep. 428.

unwilling party of a procedure which may serve no practical purpose. But they are not in the same position as *any* court, and it might well be said that they should not necessarily follow the approach taken even by the courts of the forum in deciding whether it is appropriate that a declaration should be granted.

f. Currency

The Bermuda Form provides expressly for the currency in which premiums and losses are payable: US dollars, unless the parties have agreed otherwise.⁸⁹ The contractual entitlement of a creditor to be paid in a particular currency is a substantive right,⁹⁰ and for many years this right has been recognized by way of awards made in the currency of the contract. The Arbitration Act 1996, section 48(4) gives a tribunal the power to order 'the payment of a sum of money, in any currency'. A tribunal is not entitled, however, to disregard a clear contractual provision as to the currency of payment. If it does so, the English court will interfere with the award on the basis that the tribunal has exceeded its powers.⁹¹

g. Interest

The award of interest is usually regarded in England⁹² as a procedural matter governed by English law. English law permits the award of simple or compound interest under section 49 of the Arbitration Act 1996. Where a claim is successful, interest will usually be awarded. The rate is in the discretion of the tribunal, which will normally award either simple or compound interest⁹³ at a rate that companies of a similar status as the successful claimant would have had to pay to borrow the sum awarded over the period it has been wrongly withheld. In practice, this is normally the US prime rate. The provisions in New York's Civil Practice Law and Rules⁹⁴ for recovery of simple interest at 9 per cent is clearly

⁸⁹ Condition M in the XL XS 004 version of the form. In the original Bermuda Form (form 001), the equivalent condition (n) simply stated that the premiums and losses were payable in United States currency.

⁹⁰ *Miliangos v. George Frank (Textiles) Ltd* [1976] AC 443.

⁹¹ *Lesotho Highlands Development Authority v. Impreglio SpA and others* [2003] EWCA Civ. 1159 (New Law Online case 2030714405). The court rejected the argument that the tribunal's error in failing to apply the contractual currency terms was simply an error of law which required an appeal under the Arbitration Act 1996, s. 69. The error was analysed as an excess of power on the basis that the Arbitration Act 1996, s. 48(4), which the tribunal had invoked, did not apply where the parties had made a contractual agreement as to the currency of payment.

⁹² *cf. Entron, Inc. v. Affiliated FM Ins. Co.*, 749 F.2d 127 (2d Cir. 1984) (award of pre-judgment interest treated as substantive). There is some conflict in the English authorities, but the preponderance of authority favours the view that awards of interest are governed by the *lex fori*: see the summary of the authorities in *Lesotho Highlands Development Authority v. Impreglio SpA and others* [2003] EWCA Civ. 1159 (New Law Online case 2030714405). As that case illustrates, the position becomes more complicated if the substantive law of the contract gives a right to interest. In those circumstances, the tribunal should give effect to that right, although (in the absence of agreement) the rate of interest is discretionary.

⁹³ The decision as to whether to award simple or compound interest depends upon the discretion of the tribunal. The tribunal may require evidence that a company in the position of the claimant would normally have to pay compound interest on his borrowings; or it may not wish to award compound interest for some other reason, for example because the policyholder delayed in pursuing its rights or because of some other conduct which made it reasonable for the insurer to defend the claim.

⁹⁴ CPLR § 5004.

procedural in nature, and probably will not be applied. If those provisions had been substantive, the position would be different.⁹⁵

h. Costs and Attorneys' Fees

Whether costs (both the fees and costs of the tribunal and those paid to a party's own lawyers) should be awarded is a matter of procedure, governed by English law. Early versions of the Bermuda Form contained a provision whereby each party bore its own costs of representation, and the parties shared the costs of the arbitration. Unless explicitly reconfirmed by mutual agreement after the dispute has arisen,⁹⁶ this provision is invalidated by the Arbitration Act 1996.⁹⁷ It is, of course, usual in England for the unsuccessful party to pay the successful party's reasonable costs, and those of the tribunal. Recent versions of the Bermuda Form generally make no attempt to alter this usual practice.

i. Privilege

Questions of privilege often arise in arbitrations under the Bermuda Form. The issue is usually whether the policyholder ought to be required to disclose documents generated by or for lawyers in the underlying proceedings. In principle, the question whether such documents should be disclosed is a procedural question, governed by English law. If a document, under English law principles, is privileged, the tribunal may not require its disclosure.⁹⁸ To that extent, privilege is a matter for English law. However, just because a document is not privileged to English eyes does not mean that the tribunal *must* require it to be disclosed. The tribunal has a discretion. It may sometimes be appropriate to consider foreign rules of privilege in deciding how that discretion should be exercised. A tribunal might therefore decide not to require disclosure of documents which are not privileged in England, but are privileged under some other rules. For example, where litigation is ongoing and disclosure would cause prejudice to the policyholder in the underlying litigation, the prejudice faced by the policyholder in disclosing the document might outweigh any prejudice to the insurer resulting from the document being withheld.⁹⁹

⁹⁵ See *Lesotho Highlands Development Authority v. Impreglio SpA and others* [2003] EWCA Civ. 1159 (New Law Online case 2030714405). As with their conclusion on currency, the Court of Appeal considered that if the proper law of a contract gave a substantive right to interest, an arbitral tribunal is required to give effect to that right. If they fail to do so by invoking the discretionary power in the Arbitration Act 1996, s. 49(3), this is an excess of power and not simply an error of law. There is, however, a difference between issues concerning the right to be paid interest and the rate of interest. The latter is a matter for the *lex fori* in the absence of agreement between the parties.

⁹⁶ For instance, by including a provision in an agreed procedural order.

⁹⁷ Arbitration Act 1996, s. 60.

⁹⁸ The tribunal's broad discretion over procedure does not extend to ordering disclosure of privileged documents.

⁹⁹ A detailed discussion of the practical aspects of disclosure in Bermuda Form arbitrations, including privilege, is beyond the scope of this article. These issues are, however, dealt with in *Liability Insurance in International Arbitration: The Bermuda Form*, *supra* n. *.