Interpretation of international arbitration agreements

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Introduction

As with any other contract, general rules of interpretation are crucial to ascertain the scope and reach of arbitration agreements.

This is especially important regarding non-exclusive arbitration agreements, which submit all disputes to arbitration, but include carve-out provisions that reserve the parties' right to go to court in respect of certain types of claim or relief.

In other words, the legal rules of interpretation help to determine the scope of exceptions in non-exclusive arbitration agreements. A crucial aspect in this regard is which law should apply with regard to the interpretation of arbitration agreements.

The options in this regard include the law:

- chosen by the parties;
- of the state in which judicial enforcement proceedings are pending;
- of the seat of arbitration; or
- applicable to the substantial validity of the arbitration agreement.

The choice between these options is particularly important in international arbitrations, where the parties involved are from different countries with different legal rules of interpretation and attitudes towards arbitration. Therefore, the decision on this issue should be particularly reasoned.

In the case under analysis in this update (*Medtronic USA Inc v Med Implant y Compañía Limitada*), (1) the Supreme Court, regardless of whether its final decision was right, wasted an invaluable opportunity to carry out a deeper analysis on this matter.

Facts

Medtronic USA Inc, a medical technological company, executed an exclusive distribution agreement with Med Implant y Compañía Limitada. Clause 3(7)(1) of the agreement concerns arbitration and choice of law, stating as follows:

> *"The validity, interpretation and application of this Agreement shall be governed, exclusively, by the law of the State of Minnesota. All disputes arising in relation with this Agreement shall be finally resolved by arbitration, conducted according to the rules and procedures established by the American Association of Arbitration. The English language shall be used in all and each of the arbitral proceedings. The seat of arbitration shall be Minneapolis, Minnesota, USA. Notwithstanding the foregoing, Medtronic has the right to*

seek interim injunctions and/or submit actions and seek all compensatory measures available to obtain the payment of unpaid amounts by the DISTRIBUTOR in this Agreement before any competent court or judicial body."

Medtronic sent several medical products and issued the corresponding invoices to Med Implant. However, Med Implant did not pay any of the invoices.

This led Medtronic to file a lawsuit against Med Implant before the Chilean courts, seeking the termination of the contract and the payment of $1,024,275.52 plus 1.5% in monthly interest on each invoice.

Med Implant answered the lawsuit, claiming that the Chilean courts lacked jurisdiction to hear the case because of the arbitration clause.

Decisions

The 24th District Court of Santiago rejected the jurisdictional objection, sustaining that the arbitration agreement was in favour of the US party and that, as such, it was waivable because the claimant had assumed the cost of moving to another country to file suit. Further, forcing the claimant to sue in the US would make the payment extremely difficult if not illusory, with no evident benefits for the defendant other than delaying the execution of the debt.

Med Implant appealed this decision, but the Santiago Court of Appeal affirmed it.

Finally, Med Implant issued a substantive cassation recourse against this decision before the Supreme Court.

The Supreme Court rejected the cassation, applying the Civil Code's rules of interpretation (without making this an issue). It held that the arbitration clause was clear and that contractual clauses like it should be interpreted favouring meanings under which they can produce a useful effect (according to Article 1562 of the Civil Code).

Furthering the first-instance decision, the Supreme Court held that the arbitration agreement and the choice-of-law clause had been established in Medtronic's favour and were therefore waivable. As a result, by applying the last part of the clause, Medtronic could bring an action to obtain the payment of Med Implant's debts in Chile before the Chilean courts and under Chilean law.

Finally, the Supreme Court said that the defendant's attitude was improper for a contracting party required to act in good faith because it had attempted to disavow a clause that it had approved with the goal of delaying the performance of its obligations and forcing the claimant to refile its lawsuit.

Comment

Regardless of whether the Supreme Court was right to determine that the exception to the arbitration agreement applied, the fact that it failed to analyse the issue of which legal rules of interpretation should have applied to reach this conclusion is a cause for concern. Instead, the Supreme Court simply applied (without any proper explanation) the Chilean rules of interpretation of contracts (ie, the law of the judicial enforcement forum).

However, the Supreme Court is not alone in this respect. As has been pointed out:

> "*Few courts or arbitral tribunals have addressed the question of what law governs interpretation of an international arbitration agreement in any detail. Many courts have either not considered the question of applicable law (simply interpreting arbitration agreements by reference to general principles of law) or have without explanation applied the law of the judicial enforcement forum*."(2)

The problem in this case is that the Supreme Court disregarded the choice-of-law provision that the parties had established, under which the agreement should have been governed exclusively by the law of Minnesota. The argument for doing this was that the choice-of-law clause had been established

exclusively in favour of the US party and was therefore waivable. Further, it seems that the Supreme Court made a broad application of the exception to arbitration to avoid the choice-of-law provision.

It could have been argued that the choice-of-law clause applied only to the underlying contract, as this agreement was separable from the arbitration agreement. However, this could have been disputed, as the parties probably wanted to extend the choice-of-law clause to all provisions of the contract, including its arbitration agreement.

However, it does not seem right to sustain that arbitration agreements and choice-of-law clauses are established in favour of only one of the parties when there is no express indication or evidence of this. In this case, this could be said of arbitration regarding interim injunctions and actions to obtain payment of unpaid debts in favour of Medtronic, but this point could not be sustained regarding the choice-of-law provision.

The choice-of-law provision provides certainty to both parties regarding the law applicable to a conflict and is not at the disposition of only one of them when there is no indication to the contrary, which was the case in this dispute. A proper reading of Clause 3(7)(1) provides no exception to the choice-of-law provision, but only to the scope of the arbitration agreement.

Therefore, the law of Minnesota should have been applied to interpret the scope of the arbitration agreement and the exception thereto which was established.

Notwithstanding the above, even if the parties' choice-of-law provision was to be disregarded (eg, for considering that the choice-of-law provision applies only to the underlying contract), it was improper to simply apply the law of the judicial enforcement forum for the interpretation of the arbitration agreement without any analysis or explanation, as this is a controversial matter.

An important aspect for the correct development of international commercial arbitration is the uniform enforcement of arbitration agreements, which can be accomplished only when different forums refrain from applying different local legal rules. For this reason, the direct application of the judicial enforcement forum's law for the interpretation of arbitration agreements is inadequate. This has also been highlighted by recognised authorities, which have said that:

> *"It is relatively clear that the interpretation of international arbitration agreements should not be governed by the law of the judicial enforcement forum, as some national courts have held. Rather, if a national law is to be applied, the interpretation of an international arbitration agreement should generally be subject to the law applicable to the existence and substantive validity of that agreement.*
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> *This approach would produce more uniform results than application of the law of the judicial enforcement forum (which would vary depending on where litigation is brought) and would in most cases more closely accord with the parties' intentions. This result is also consistent with most choice-of-law authorities in other contexts*."(3)

Therefore, even though the Supreme Court's decision was probably correct in this case (as it allowed Medtronic to bring an action to obtain the payment of its unpaid credit), it missed the chance to provide a sharper and more sophisticated decision concerning the applicable legal rules of interpretation of arbitration agreements, which is a crucial matter for the uniform enforcement of international commercial arbitration agreements.

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Endnotes

(1) Supreme Court, March 2 2017, *Medtronic Usa Inc v Med Implant y Compañía Limitada,* Case 47,923 2016.

(2) Born, Gary, *International Commercial Arbitration* (2nd ed, Wolters Kluwer 2009) p1394.

(3) *Ibid,* p1397.
