UNIVERSITY OF TECHNOLOGY, SYDNEY

DOCTOR OF JURIDICAL SCIENCE DEGREE COURSE

DOCTORAL DISSERTATION

International Commercial Arbitration and Public Policy

(With principal reference to the laws of Australia, France, Switzerland, the United Kingdom and the United States)

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CERTIFICATE OF AUTHORSHIP / ORIGINALITY

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CONTENTS

ABSTRACT

The paper examines the evolution of the recognition and enforcement of "foreign" arbitral awards prior to the introduction of the various international arbitration conventions by referring to court decisions of the relevant countries, primarily the United States and the United Kingdom. The scope and importance of the New York Convention will be canvassed, with specific reference to cases.

The Dissertation traces the evolution of judicial and legislative attitudes towards arbitration (in particular, the issue of arbitrability), from the original position of antipathy towards arbitral processes, to the active promotion of arbitration and a "hands-off" approach to its processes by legislators as well as courts.

The introduction of the arbitral process to developing countries will be discussed in the context of some recent controversial arbitrations in Indonesia and Pakistan.

Public policy as the criterion for the enforcement of awards by national courts will be discussed and relevant authorities referred to. The reasoning adopted by courts in this area will be examined and discussed.

The paradigm shift in the enforcement of awards and the leeway granted within the parameters of the arbitral decision making process will be highlighted by two case studies. Both demonstrate clearly the current negation of public policy considerations. The first is a decision of the English Court of Appeal [1] which was mirrored by a subsequent arbitration award [2] in which the discarding of public policy considerations was particularly remarkable as constitutional issues were involved, which normally would have given rise to the expectation of deliberations as to the notions of public policy.

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1 *Westacre Investments Inc v Jugoimport-SPDR Holding Co Ltd and ors* [1999] 3 WLR 811.

2 *Sandline International Inc v Independent State of Papua New Guinea*, International law Reports (2000), Volume 117, 552.

NOTE CONCERNING "UNITED KINGDOM" AND "ENGLISH" LAW

The title of the Dissertation *inter alia* refers to the " . . . laws of . . . the United Kingdom." Within the text, there are references to both the "United Kingdom" and "England." The constitutional and legislative position in the United Kingdom is perhaps more complex than in other jurisdictions and a brief outline is necessary.

United Kingdom Parliament

Parliament is called the "Parliament of the United Kingdom of Great Britain and Northern Ireland." (Great Britain is comprised of England, Scotland and Wales). The United Kingdom Parliament comprises the monarch, the House of Lords and the House of Commons. [3]

Until relatively recently, Parliament was regarded as the supreme law-making body within the United Kingdom; however, European Community law is now paramount within the United Kingdom's constitutional framework. [4]

The legislation of the United Kingdom Parliament is presumed to apply to the whole of the United Kingdom, although there can be an express or implied exclusion of a part of the United Kingdom from the operation of a particular Act. [5]

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3 Halsbury's *Laws of England*, Fourth Edition Reissue, Volume 34, 1997, at paragraph 501.

4 Halsbury's *Laws of England*, op cit, Volume 8(2), paragraph 1.

5 Halsbury's *Laws of England*, op cit, Volume 44(1), paragraph 1318. For example, the *Arbitration Act* 1996 (UK) applies in England and Wales, and Northern Ireland, although provisions relating to consumer arbitrations apply in Scotland. The general commercial arbitration law applying in Scotland is the *Arbitration Act* 1975 (UK). The latter Act was repealed in England and Wales and Northern Ireland, by the *Arbitration Act* 1996 (UK).

Legal systems

England and Wales have the one legal system. [6] As from the Sixteenth Century, "English law" has prevailed in Wales. [7] Scotland has a distinct legal system and its own courts, with, in civil matters, rights of appeal to the Appellate Committee of the House of Lords. [8]

Northern Island also has its own courts, with rights of appeal to the House of Lords in both civil and criminal matters. [9]

Devolution

The United Kingdom Parliament has legislated for the devolution of power to regional assemblies - to the Scottish Parliament, the Northern Island Assembly and the National Assembly for Wales. [10]

The Scottish Parliament has the power to pass primary legislation, subject to certain subject matters being reserved by the United Kingdom Parliament. The Northern Ireland Assembly also has power to enact primary legislation, but the Northern Ireland Assembly is also presently suspended. The National Assembly for Wales has no power to enact primary legislation - that power remains with the United Kingdom Parliament. [11]

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6 Halsbury's *Laws of England*, op cit, Volume 8(2), paragraph 41.

7 Halsbury's *Laws of England*, op cit, Volume 8(2), paragraph 42, n.2.

8 The general commercial arbitration law applying in Scotland is the *Arbitration Act* 1975 (UK). The latter Act was repealed in England and Wales and Northern Ireland, by the *Arbitration Act* 1996 (UK).

9 Halsbury's *Laws of England*, , op cit, at paragraphs 52, 60 and 67.

10 Via the *Scotland Act* 1998 (UK), the *Northern Ireland Act* 1998 (UK) and the *Government of Wales Act* 1998 (UK).

11 For a detailed discussion of these issues, see Burrows, *Devolution*, Sweet & Maxwell,, 2000.

Consequently, at present, the Scottish Parliament alone has power to pass legislation which has equal force to that of the United Kingdom Parliament. [12]

Dissertation

In relation to the expressions used in the Dissertation; generally, references to legislation will be referred to as United Kingdom legislation, as Parliament is the United Kingdom Parliament.

It should also be noted that it is the United Kingdom which is the contracting State to the New York Convention.

References to decisions of the House of Lords and the Court of Appeal will be described as "United Kingdom" and "English" decisions respectively. As noted above, whilst each of Scotland and Northern Ireland has its own courts, there are rights (in the case of Scotland, in civil matters only). of appeal to the House of Lords. The House of Lords, consequently, hears appeals from the whole of the United Kingdom.

The English Court of Appeal is the Court of Appeal for the unitary system of England and Wales. Given that "English law" was historically also the law of Wales, it is more appropriate to refer to decisions handed down by it as "English" decisions. Decisions of other Courts (such as Queen's Bench and Chancery) will also be referred to as "English" decisions.

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[12] In this context, it might be noted that the Scottish Council for International Arbitration has prepared a draft *Arbitration (Scotland) Bill*, which has yet to be introduced to the Scottish Parliament. One of the provisions of the draft Bill, if enacted, would repeal the *Arbitration Act* 1975 (UK) – see *scia.co.uk*.

ABBREVIATIONS

Convention/New York Convention	The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958).
ECOSOC	United Nations Economic and Social Council.
GATT	General Agreement on Trade and Tariffs.
ICC	International Chamber of Commerce.
ICC RULES	Arbitration Rules of the International Chamber of Commerce.
IMF	International Monetary Fund.
OECD	Organisation for Economic Cooperation and Development.
PICJ	Permanent International Court of Justice.
UN	United Nations.
UNCITRAL	United Nations Commission on International Trade Law.
UNCITRAL Model Law	UNCITRAL Model Law in International Commercial Arbitration.

UNCTAD	United Nations Commission for Trade and Development.
UNIDROIT	International Institute for the Unification of Private Law.
USC	United States Code.
WTO	World Trade Organisation.

PREFACE AND OUTLINE

"*Today, international commercial arbitration has a new prominence.*" [13]

Principal issue

The principal issue addressed in the Dissertation concerns the selective application of public policy and the potential harm to the emerging global society as a result of the increasing negation of public policy in international commercial arbitration.

The negative effect follows from the reading down of public policy particularly in the process of enforcement of awards. Leading courts, such as those of the United States seem to have turned away dramatically from public policy considerations in the decision making process, which previously had been viewed as part of a well established doctrine within the law.

The reasons behind this change must - after careful consideration - be seen as a consequence of the shift in attitude towards public policy generally, following in the wake of the broad interpretation of privatisation policies at national and international level which has resulted in a general reading down of public policy evaluations within a specific societal framework, elevating private interests by raising their strict enforcement to paramount importance. Courts and arbitral tribunals are following this ground-breaking shift both at State level and internationally.

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[13] UN Secretary-General Annan, "Opening address commemorating the successful conclusion of the 1958 United Nations Conference on International Commercial Arbitration", *Enforcing Arbitration Awards under the New York Convention Experience and Prospects*, UN Publication E.99 V.2

International commercial arbitration

Commercial arbitration is an important part of the complex structure of international trade. As a dispute resolution mechanism, arbitration fulfils a "widespread need", both on a domestic and international level. It has become the preferred method of dispute settlement in international commercial transactions. [14]

As the volume of international trade and commerce has increased manyfold in recent years [15], arbitration has consequently grown significantly in importance. The "huge growth" in the "volume and complexity" of arbitration has prompted initiatives at all levels – "national, regional and international", in order to facilitate the arbitral process. [16] International institutions have been established and international conventions have been developed to assist the processes of arbitration. [17] Countries such as those selected for representative analysis in the Dissertation have amended their arbitration laws to make arbitration more accessible and less subject to control by courts. [18]

Interestingly, arbitration was not always held in such high regard. Initially, courts in jurisdictions such as England and the United States were reluctant to condone private arbitration. [19] If powers of adjudication were conceded at all, Courts astutely reigned in those powers by limiting the scope of the subject matter which parties could submit to arbitration.

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14 Lew, *Applicable Law in International Commercial Arbitration,* Oceana, 1978, 1.

15 Giddens, *Runaway World,* Routledge, 2000, at 28.

16 ibid.

17 An example of such an institution is the ICC Court for International Arbitration; probably the best known and most widely accepted convention is the *Convention on the Recognition and Enforcement of Foreign Arbitral Awards* 10 June 1958 (the "New York Convention"); the New York Convention was followed by the *UNCITRAL Model Law in International Commercial Arbitration.*

18 Eg, the United Kingdom *Arbitration Act* 1979; Chapter 12 of Switzerland's Private International law [*Loi fédérale sur le droit international privé* (1989)]; in France, the Decree of 12 May 1981 (*Décret n. 81-500 du 12 Mai 1981*), which introduced new provisions into the French *Code Civile.*

19 For a discussion of earlier judicial attitudes to arbitration, see Mason P, *Changing Attitudes in the Common Law's Response to International Commercial Arbitration,* International Conference on International Commercial Arbitration, Sydney, 19 March 1999.

Judicial and legislative attitudes have changed, resulting in commercial arbitration now being favoured and promoted. Not only has new "arbitration-friendly" legislation been enacted in many jurisdictions (including those selected for analysis in the Dissertation), but some courts have gone so far as to pull back from their supervisory role by reading down the public policy defence available under the New York Convention [20] and by issuing judicial guidelines actually imposing restrictions on their supervisory role in appeals from arbitral proceedings and awards. [21]

With regard to specific aspects of arbitration, due consideration is to be given to the following issues:-

(i) Arbitrability

Courts (and legislatures) have at times imposed exclusions on certain subject matters from arbitration. For example, in the United States, antitrust matters and remedies relating to the purchase of securities were initially regarded as non-arbitrable. The United States Supreme Court, however, altered its position over time and removed the previous bar on the arbitration of such matters. [22]

(ii) The application of public policy by arbitrators in the making of awards

As the scope of subject matter which may be submitted to arbitration widens and at the same time the formal supervising control of courts is reduced, the question must be posed, if the legal systems – which overall are needed to guarantee a structured balancing between rights and obligations on the basis of legal principle – are being unhinged by the new evolutionary process which favours the seemingly open-ended protection of private rights at the cost of any relevant analysis of the wider

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20 Article V.2(b) of the New York Convention provides that recognition and enforcement of an award may be refused if such recognition or enforcement would be contrary to the public policy of the forum State.

21 See, eg, the United Kingdom decision, *Pioneer Shipping Limited v BTP Tioxide Ltd* [1982] AC 724, where the House of Lords laid down the "Nema guidelines", concerning appeals from arbitral awards under the United Kingdom *Arbitration Act* 1979.

22 See *Mitsubishi Motors Corp v Soler Chrysler-Plymouth Inc* 473 US 614 (1985) on anti-trust matters; and *Scherk v Alberto-Culver* 417 US 506 (1974), *Dean Witter Reynolds Inc v Byrd* 470 US 213 (1985) and *Rodriguez De Quijas v Shearson/American Express* 490 US 477 (1989) on securities law.

consequences for societal development as a whole – if this is not undermining the very purpose of the inclusion of public policy considerations in the adjudicative process.

(iii) Enforcement of awards

The enforcement of awards is largely governed by the relevant Conventions.

The reading down of the public policy defence in relation to the enforcement of awards has become so pronounced in jurisdictions such as the United States, that the statutory defence has been virtually negated. [23] Such an approach is at odds with the very concept of public policy. To fetter or restrict public policy means that legal systems are potentially falling victim to untrammelled private interests.

In order to understand the significance of the role of public policy as a vital constituent part of any legal system on which a democratic system rests, the following notions must be canvassed:-

"Threshold" issue

What role should public policy play in what is essentially a private process? Arbitration requires parties to a dispute appointing a trusted third party (the arbitrator) to resolve their dispute, instead of enlisting a court. The arbitrator's authority is based on a contract - the private agreement between the parties. It might, therefore, be said that the immediate parties to a dispute are the only ones with an interest in the resolution of the specific dispute and the enforcement of any resultant award.

As arbitrators are bound to apply the law (which includes public policy), public policy does have (indeed *must* have) a significant role in the processes of arbitration. Because of this, ascertaining and where necessary, balancing, competing public

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[23] In *Parsons & Whittemore Overseas Co Inc v Societe Generale de L'Industrie du Papier (RAKTA)* 508 F.2d 969 (Second Circuit, 1974), the Court held that the public policy defence in the New York Convention should, because of the Convention's "pro-enforcement bias", be "construed narrowly." (at 973-74.)

interests is part of the overall function of the arbitrator. The arbitrator must apply the most appropriate public policy principles to the dispute at hand. That may be the public policy of the law applicable to the arbitration, the law of the forum of the arbitration, or of the likely place of enforcement of the award, or even international public policy. [24] "International" public policy has been described as not being concerned with purely national influences, but rather with "fundamental standards" of the international community, covering both trading standards and humanitarian concerns. [25]

In choosing the applicable public policy, arbitrators must firstly have regard to (and, where necessary, apply) the public policy of the jurisdictions "whose national interests are substantially involved" in the matter under arbitration. [26] International public policy can override national interests, however, and it is for the arbitrator to decide in each case whether, given the subject matter and the interests involved, international pubic policy should be applied. [27]

Public policy

Public policy is of vital importance – it is the judicial benchmark for the protection of the public interest. [28] It determines the application of the law and shapes its development.

Judges and arbitrators have a clear duty to have regard to public policy considerations and to apply public policy principles where the public interest would otherwise be offended. [29] As noted above, the public policy which is to apply will depend on the context and subject matter involved and the relationship of those to both national and international public policy.

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24 Lew, op cit, at 83.

25 Lew, ibid.

26 Chukwumerije, *Choice of Law in International Commercial Arbitration*, Quorum Books, 1994, at 183.

27 Chukwumerije, op cit, at 194.

28 For discussions on the history and importance of public policy, see Winfield, "Public Policy in the English Common Law" (1928) 42 *Harvard Law Review*, 76 et seq; Knight, "Public Policy in English law", (1922) 38 *Law Quarterly Review*, 207 et seq; Stone, *The Province and Function of Law*, Maitland Publications, 1950, at 494 et seq.

29 Stone, op cit, 500.

Major points

It was noted above that the approach by Courts in jurisdictions such as the United States and United Kingdom has been to broaden considerably the concept of arbitrability and, at the same time, to narrow considerably the scope for courts to intervene in arbitral processes, including the enforcement of awards.

Consequently, at present, practically any type of dispute may be arbitrated. Further, as courts restrict their supervisory function with the enforcement of awards, this leads potentially to a derogation of the courts' constitutional functions, conceptualised as safeguarding citizens from the abuse of power.

The result of the emerging trend to read down or completely negate public policy in some jurisdictions may ultimately do harm to the process of "privatising" the adjudicative process.

Arbitrators do not have to be lawyers. Consequently, they do not have the duties of lawyers as officers of the court. Their selection is not transparent. Arbitrators also have a significant financial self-interest and might, hence, be tempted to favour economically stronger parties as the more likely providers of future appointments. In addition, as the appointment of an arbitrator is by private treaty, an arbitrator may be less inclined to venture into the arena of public policy considerations.

Globalisation

The present developments in arbitration reflect the processes of "globalisation", the main feature of which is the pressure for the liberalising of trade relationships. Globalisation mandates greater certainty in the enforcement of international transactions and promotes the tendency to sidestep public policy issues, because of the non-specificity of the issues involved when viewing society as "global."

One of the principal advocates for a strict limitation of public policy considerations, particularly in the enforcement of awards, is the United States. The latter is also at the forefront to move towards a more liberalised global trade regime. It is the world's largest economy and has the greatest number of the world's largest corporate entities. [30] Further, the United States has always used institutions such as the GATT and WTO to pursue its own interests, which are further enhanced by a rising number of bilateral "free trade" agreements.

Ensuing is the privatisation of dispute settlement through arbitration, which is being promoted as the favourite option for national and international commercial dispute resolution, because it allows for the exclusion of any specific societal public policy considerations. This is cogently promoted by the United States as an achievement in the ongoing pursuit of global trade liberalisation, potentially securing its continued dominance. [31]

Recommendations

The traditional courts should reconsider their duty to shape public policy considerations. Arbitrators, in usurping the position of judges, must not totally negate public policy considerations, if the pursuit of a "global society" is to achieve more than an unsubstantiated slogan.

An institution which secures the promotion and vetting of an "international" public policy, such as an international court for international commercial arbitration is to be proposed, as public policy is an ongoing process, not a specific fixed notion.

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30 In 2002, the United States GDP (expressed in millions of USD) was 10,383,100. That of its nearest rival, Japan, was 3,993.433 (source - World Bank www.worldbank.org). The United States also had nearly 40% of the world's 500 largest companies (source - *www.fortune.com*).

31 Pengilly, "United States Trade and Antitrust Laws: A Study in International Legal Imperialism From Sherman to Helms Burton", 6 (1998) *Competition and Consumer Law Journal*, 187, at 188.

Jurisdictions whose laws and cases will be referred to

Foremost, the laws and cases of Australia, France, Switzerland, the United Kingdom and the United States and will be referred to. The reasons for choosing these jurisdictions are:-

- France, Switzerland, the United Kingdom and the United States host important arbitration centres. Aksen notes that by the 1970s, various centres had started competing to "attract arbitration." [32] Traditionally, London and Switzerland were the places to which most parties turned to schedule international commercial arbitral hearings. [33] The factors involved in those choices were, respectively, London's position at the centre of maritime, insurance and commodity trade and Switzerland's political neutrality and secrecy laws.

  Aksen states that both centres started to lose some attraction, however, and other jurisdictions (such the United States) have risen in importance. [34] The response from both the United Kingdom and Switzerland was to become more "arbitration friendly" by enacting new arbitration legislation. [35] In each case, the ability of parties to appeal from arbitral proceedings was significantly curtailed. This resulted in the Courts of these jurisdictions largely stepping back from their supervisory role.

- As far as institutional arbitration is concerned, the ICC [36] notes that between 1989 and 1999, the leading centres chosen by parties for arbitrations (by way of percentage of the total number of cases referred to the ICC Court for International Commercial Arbitration) were:-

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32 Aksen, "International Arbitration - Its Time Has Arrived!" *Case Western Reserve Journal of International Law*, Volume 14, Number 2 (Spring 1982), 247, at 250.

33 ibid.

34 ibid.

35 In the United Kingdom, the *Arbitration Act* 1979; in Switzerland, the *Loi federale sur le droit international privé*.

36 The ICC is the primary international institution for commercial arbitration - "No other institution approaches ICC's universality and volume of cases." (Craig, Park and Paulsson, *International Chamber of Commerce Arbitration*, Third Edition, Oceana, 2000, at 3).

- Paris - 33%;
- Switzerland - 25%;
- United Kingdom – 8.5%; and
- United States - 5.25%.

The total number of such cases during that period was 11,143. [37]

- The Australian jurisdiction is also analysed as efforts are being made to promote it as a regional centre for international commercial arbitration. In 1990, Australia was described as relying on its political stability and well regarded legal system in order to become a regional centre for international commercial arbitration. [38] The desire to attract commercial arbitration business to Australia has undoubtedly been driven by the growth in arbitrations emanating from the Asia-Pacific region, which has been considerable. Between 1983 and 2000, parties from Asia in ICC arbitrations increased from 3.1% to 15.2% and exceeded 16% if Australia was included. [39]

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37 Craig, Park and Paulsson, op cit, at 4.

38 Street, "Dispute Resolution in the Asia/Pacific – Practice Sites and Centres – Australia", paper presented to the American Arbitration Association Conference "Facilitating International Business: Dispute Resolution in the Asia/Pacific Region", San Francisco, 21-22 September 2002.

39 Pryles, "The Growth of International Arbitration", paper presented to Federal Attorney-General's Department 24th International Trade Law Conference, Canberra, 9 Ocober 2002.

PART I

THE ENFORCEMENT OF ARBITRAL AWARDS PRIOR TO THE NEW YORK CONVENTION

THE NEW YORK CONVENTION AND UNCITRAL MODEL LAW

THE ADOPTION OF THE CONVENTION AND MODEL LAW – SOME ASSOCIATED ISSUES

CHAPTER I

THE ENFORCEMENT OF ARBITRAL AWARDS BEFORE THE NEW YORK CONVENTION

> "*More important for the exporter is the question whether an English award can be enforced in a foreign country . . . or vice versa, whether a foreign award can be enforced in the English jurisdiction. As matters stand at present, it is not possible to give a generally valid answer to this question. The methods of execution of an overseas award are different in the various countries . . .*" [1]

A. Recognition of arbitral awards

How were awards enforced prior to the New York Convention?

The ability to enforce a validly obtained award is a crucial issue. Arbitration panels, unlike courts, do not have the "legal authority to compel" [2] the enforcement of, or conformity with, their awards.

David notes that arbitration originally developed, however, without a specific enforcement mechanism in support of awards. This was the case in Roman Law. If an award was not obeyed, the only resort was to rely on the penalty provisions in the parties' original agreement. [3] The penalty provisions were enforced upon default, rather than the award itself.

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1 Schmitthoff, *The Export Trade*, Second Edition, Stevens and Sons, 1950. This quote has been chosen to reflect the position prior to the advent of the New York Convention in 1958.

2 von Mehren, "The Enforcement of Arbitral Awards under Conventions and United States Law", *The Yale Journal of World Public Order*, Volume 9, 1983, 343, at 344.

Penalty provisions or bonds, of course, also became a feature of English law. An example of the use of such a provision in the context of an arbitration is *Vynior's* case. [4] The parties had appointed an arbitrator, after which the defendant (who had agreed upon a bond to abide by and perform any arbitral award), revoked the arbitrator's authority. It was held that the revocation was lawful, as a party could not make his or her act not able to be countermanded. It was therefore permissible to terminate the arbitrator's authority. The plaintiff, however, was able to recover on the bond, as the defendant had, by such revocation, breached the agreement to abide by any award.

The use of bonds, of course, came to be regarded as unsatisfactory, as, frequently, the amount stipulated had little or no relationship to the actual amount of damage suffered.

Sayre states [5] that in 1687 (sic), the *Statute of Fines and Penalties* 8 & 9 William III was enacted, which prohibited the recovery of the amount payable under a bond, except in cases where the amount of actual damages suffered justified recovery. This, says Sayre, had a significant effect on arbitration, as, usually, the plaintiff could not establish that any damage had been suffered by a refusal to arbitrate. [6]

Sayre also notes that the first arbitration statute [7] was passed "the following year" (see n. 6 below) which provided for submissions to arbitration to be made orders of court, revocation accordingly being regarded as a contempt.

It is interesting to note the preamble to the statute, in which is set out the perceived advantages of arbitration - it was seen as "promoting trade" and the making of court orders in relation to submissions to arbitration would render "the awards of

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3 David, *Arbitration in International Trade*, Kluwer, 1985, at 366.

4 8 Co. Rep. 81b.

5 Sayre, "Development of Commercial Arbitration Law", *Yale Law Journal*, Volume XXXVII (1927-1928), 595.

6 The year quoted by Sayre (1687) is incorrect. The statute referred to was passed in 1697 and, *inter alia*, dealt with actions on bonds - *Frivolous and Vexatious Suits*, 8 & 9 Will. III. Ch. 11. It provided that, in any action on a bond, the plaintiff could assign as many breaches as the plaintiff wished; also, that in any action on a bond, the jury was required to assess damages on breach.

7 *An Act for Determining Differences by Arbitration*, 9 & 10 William III Ch. XV.

arbitrators the more effectual . . . for the final determination of controversies referred to them by merchants and traders."

The development of modern arbitration

At the start of the eighteenth century, it seemed that the practice of international arbitration between States, had fallen into disuse. Simpson and Fox state [8] that this changed in 1794 when the modern development of international arbitration between States commenced with the conclusion of the Jay Treaty [9] between the United States and England. The Treaty settled most of the outstanding matters between the two countries following the Declaration of Independence in 1776. Those matters not settled by the Treaty were referred to arbitration. A series of mixed commissions were established, one of which was required to deal with "allegations of judicial obstruction" in the collection of debts owed to British creditors, whilst another Commission was appointed to deal with claims arising out of the seizure of ships and cargo (by both sides) during England's war with France. [10] The governments of both countries undertook to reimburse merchants for their losses. The proceedings of the Commission charged with investigating judicial obstruction were unsuccessful, the Commission breaking up in 1799; the other Commission, however, proceeded to make a number of awards.

As for awards made arising out of arbitrations between private parties, these came to be recognised and enforced by municipal courts, on virtually the same grounds that applied in respect of domestic arbitrations. The courts of various jurisdictions, in considering whether to enforce awards turned to contractual principles. [11] An award was regarded as arising out of the contract between the parties (ie, the agreement to submit to arbitration and to observe the provisions of any award arising out of that submission). The party favoured by the decision could apply to the courts of the

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8 Simpson and Fox, *International Arbitration*, Stevens & Sons, 1959, at 1.

9 The General Treaty of Amity, Commerce and Navigation. The name "Jay" arises from John Jay, the first Chief Justice of the United States and special envoy to the United Kingdom in 1794-95.

10 Simpson and Fox, *op cit*, at 1 and 2.

11 Lorenzen, "Commercial Arbitration - Enforcement of Foreign Awards", *45 Yale Law Journal* (1935-36) 39, at 44.

jurisdiction where enforcement was sought, for a judgment to be entered on the basis of the award.

Whilst some jurisdictions had enacted legislation covering arbitrations, municipal legislation generally did not make provision for the recognition and enforcement of awards other than domestic awards.

Enforcement of foreign judgments at common law

Prior to the enactment by States of statutes which recognised foreign judgments (usually on the basis of reciprocity), municipal Courts had also started to develop rules to deal with the enforcement of foreign judgments. In *Williams v Jones* [12], in which a party sought to enforce a foreign judgment in England, Parke B. said:-

> "Where a court of competent jurisdiction has adjudicated a certain sum to be due from one person to another, a legal obligation arises to pay that sum, on which an action of debt to enforce the judgment may be maintained. It is in this way that the judgments of foreign and colonial courts are supported and enforced." [13]

In 1870, in the decision in *Godard v Gray* [14], the Court of Appeal affirmed this principle and reviewed some of the circumstances in which a court might refuse enforcement. These included: a lack of jurisdiction on the part of the tribunal which pronounced the judgment, or where the judgment may have been obtained by fraud, or where the foreign court had "knowingly and perversely disregarded the rights given to an English subject by English law" [15]. On the same day as that judgment, the Court of Appeal handed down the decision in *Schisby v Westenholz* [16], which related to whether a judgment obtained in Paris could be enforced in England. Blackburn LJ referred to the judgment of Parke B in *Williams v Jones* with approval, stating that the

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12 (1845) 13 M & W 628,
13 op cit, at 633.
14 Law Rep 6 QB 139.
15 at 149, per Blackburn LJ.
16 Law Rep 6 QB 155.

applicable principle was that a judgment of a court of competent jurisdiction over a defendant:-

> " . . . imposes a duty or obligation on the defendant to pay the sum for which judgment is given, which the courts in this country are bound to enforce . . . the principle on which foreign judgments were enforced was that which is loosely called 'comity' ". [17]

There was, naturally, some qualification to this principle:-

> " . . . anything which negatives that duty, or forms a legal excuse for not performing it, is a defence to the action." [18]

In this case, the defendants conceded that the judgment in Paris had been legally obtained. [19] Whilst they were found by the jury to have had adequate notice of the proceedings, they were not residents of France. They had not been within the jurisdiction of France when the contract was made, nor when the suit commenced, nor when judgment was entered. The Court of Appeal held that, consequently, the defendants were not under any obligation to obey French law. Because of this, the (England) Court would not order that judgment be enforced.

In *Nouvion v Freeman* [20], a decision of the House of Lords, Lord Herschell said (*obiter*) that there was "no doubt" that in English courts, effect would be given to a foreign judgment, so long as the judgment was "final and conclusive . . . so as to make it res judicata between the parties." [21] There were some exceptions, of course. A judgment obtained by fraud could not be enforced. This principle was extended

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17 at 159.

18 ibid.

19 The law of France at that time permitted a kind of substituted service of process in cases where foreigners were being sued. The summons was served on the *Procureur Imperial* and the foreign defendant had one month in which to appear. If at the end of the month the defendant had not appeared, judgment was entered. Judgment did not become final and conclusive for a further two months, during which time the defendant could enter an appearance.

20 (1889) 15 App. Cas. 1.

21 op cit, at 8.

even to where the issue of fraud had been considered and rejected by the court in the original jurisdiction. [22]

In the United States, similar considerations arose. The Supreme Court in *Hilton v Guyot* [23] said that the courts, in considering whether to allow enforcement of foreign judgments:-

> " . . . must obtain such aid as they can from judicial decisions, from the works of jurists and commentators and the acts and usages of civilised nations." [24]

Gray J (delivering the majority opinion) noting that law had no effect "beyond the limits of the sovereignty from which its authority is derived" [25] said that the extent to which the laws of one nation are allowed to operate within the dominion of another (whether by executive decree, legislation or court order) depends upon the "comity of nations." Whilst comity is neither an absolute obligation, nor "mere courtesy or goodwill", it is the recognition which:-

> " . . . one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience and to the rights of its own citizens . . ." [26]

The doctrine of comity, therefore, according to the United States Supreme Court, involves balancing the recognition of the formal processes of another State, with the rights of United States citizens. Further, comity, as extended, is that "of the nation". This would follow from the fact that those things to which recognition is extended (eg, acts, determinations or processes) are founded in or emanate from the formal structures of other States.

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22 *Abouloff v Oppenheimer* 10 QB 294. The decision has been criticised, although it has not been overruled.. In *Westacre Investments Inc v Jugoimport-SPDR Holding Co Limited* [1999] 3 WLR 811, Waller LJ in the Court of Appeal noted that the House of Lords had, in *Owens Bank Limited v Bracco* [1992] 2 AC 443, felt unable to overrule *Abouloff*, but, as Waller LJ continued - " . . . it is a decision which has been distinguished and its application weakened wherever possible." (*Westacre v Jugoimport*, op cit, at 826).

23 159 US 113 (1895).

24 op cit, at 163.

25 ibid.

26 op cit, at 164.

In other words, comity has a distinct public character.

Gray J then stated that, in relation to a judgment of the courts of another country, where a full and fair trial had been conducted before a court of competent jurisdiction, where the defendant had appeared voluntarily (or had been duly cited) under a system of jurisprudence "likely to secure an impartial administration of justice" between citizens of its own country and those of another and where there was no prejudice in the court or fraud in the obtaining of the judgment, then the merits of the case would not be "tried afresh" and the judgment could be enforced. [27]

Arbitral awards at common law

The way in which courts then approached the enforcement of foreign arbitral awards was based on different considerations, but, it is submitted, with one common thread - that of duty. The duties in each case, however, are of quite a different nature.

As noted in *Hilton v Guyot* [28], the doctrine of comity imposes "an international duty" (albeit not an absolute one), which requires States to recognise the formal acts, orders and decrees of other States.

In private arbitrations, there is no executive or judicial authority underlying the process. States may legislate for the facilitation of arbitration and courts may exercise some degree of control over arbitral processes, but an arbitral award is a private determination, the authority for which flows from the contractual relationship between the parties. The requisite duty, consequently, of parties under contract to honour the requirements of their agreement to arbitrate and to observe the terms of the resultant award.

In *Purslow v Bailey* [29], Holt CJ (of King's Bench) stated that a submission to arbitration is an:-

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27 At 203.
28 op cit, at 164.
29 2 Ld. Raym. 1039.

> " . . . actual mutual promise to perform the award of the arbitrators". [30]

It was seen that losing parties ought to abide by arbitral awards. Enforcement of awards was undertaken by the Court of Chancery. The performance of an award could be:-

> " . . . compelled in equity, on the ground that the award only ascertains the terms of a previous agreement between the parties." [31]

This is confirmed by authorities such as *Wood v Griffith* [32], in which Eldon LC held it was clear that a bill would lie for the specific performance (an equitable remedy) of an award, for the award "contains nothing more than an agreement, on terms which a third person points out." In *Nickels v Hancock* [33], Knight Bruce LJ stated that the remedy for non-observance of an award was analogous to specific performance.

The consensual nature of commercial arbitration was recognised by Lord Bramwell in His Lordship's draft *Arbitration Code*, prepared in the 1880s with the backing of the Corporation of the City of London and the London Chamber of Commerce. The idea behind the *Arbitration Code* was that, because of the territorial limits on municipal legislation (and the jurisdiction of the courts), it was argued that the only form of arbitration with the potential to become "international" was consensual arbitration. As this form of arbitration is based on the agreement of autonomous (private) parties, there is no barrier to limiting the effect of arbitration agreements and awards to particular territories or States. [34]

Lord Bramwell's code was not taken further, although the *Arbitration Act* 1889 (UK) did reflect the essentially contractual foundation of private arbitration.

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30 op cit, at 1040.
31 Tomlins *The Law-Dictionary*, 4th Edition, 1835, by T C Granger (numerous publishers)
32 (1818) 1 Wils. Ch 44.
33 (1855) 7 DM & G 300.
34 Hunter, Marriott and Veeder (eds) *The Internationalisation of International Arbitration*, Graham & Trotman/Martinus Nijhoff, 1995, at 13.

An early England case involving a request to enforce a foreign arbitral award was *Merrifield, Ziegler & Co v Liverpool Cotton Association* [35], in which a German company ("Hapke") sought the enforcement in England of an award given in Germany, following an arbitration held under the rules of the Bremen Cotton Exchange. The plaintiffs were members of the Liverpool Cotton Association (the "Association"). Under the rules of the Association, members could be expelled for any dishonourable or disreputable conduct in their dealings with members of other associations with which the Association had entered into arrangements or undertakings. The Association had previously entered into an arrangement with the Bremen Cotton Exchange, under which it was agreed, *inter alia*, that refusal to refer disputes to arbitration, or to abide by an arbitral award, constituted dishonourable or disreputable conduct.

The plaintiffs and Hapke had entered into a contract (containing an arbitration clause) for the shipping of cotton. Hapke claimed that the plaintiffs had failed to ship the cotton as provided for and called for arbitration. Hapke appointed their arbitrator and called on the plaintiffs to nominate theirs. The plaintiffs ignored these requests. Nevertheless, the arbitration proceeded. An award was made in their absence. The Association then threatened to expel the plaintiffs, as their conduct was deemed disreputable by their refusing to submit to arbitration. The plaintiffs then commenced an action in the Chancery Division (joining both Hapke and the Association), seeking, *inter alia*, orders that they had not engaged in such conduct and further, that the award was invalid, or unenforceable.

Hapke counter-claimed for a money judgment based, not on the original contract between the parties, but on the fact of the award. (Domestic awards in England were subject to the *Arbitration Act* 1889, s12 of which provided that such awards, by leave of the Court, could be enforced "in the same manner as a judgment or order to the same effect").

Eve J considered what the effect of the award was in Germany. The German Code of Civil Procedure provided that an arbitral award, as between the parties, had the effect

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[35] (1911-1912) The Law Times Reports, Volume CV, 97.

of a final judgment as pronounced by a court of law. In relation to the treatment of foreign awards in Germany, Hapke's expert witnesses gave evidence that the law that applied in Germany was that courts enforced foreign awards on the basis of contract, in that the submission to arbitration implied an agreement to observe and carry out the award.

The plaintiff's expert witnesses disputed this and Eve J said that he could not find that Hapke had conclusively proven that their submissions reflected the law of Germany.

Eve J said that the only point was whether the award was a decision which the High Court of England " . . . ought to recognise as a foreign *judgment*". [36] (emphasis added). It is unclear why His Honour used the expression "judgment", when, what was before the Court of Chancery, was an application to recognise and enforce an award.

Perhaps His Honour had regard to the provisions of the German Code of Civil Procedure, which provided that an award " . . . has the *effect* of a final judgment." [37] (emphasis added). This was in similar terms to s12 of the *Arbitration Act* 1889. The award was not itself a judgment; rather, it had the same effect as a judgment.

In any event, Eve J held that the award, despite being " . . . conclusive as to all matters thereby adjudicated upon", could not be enforced in England. This was because, His Honour said, it could not at that stage have been enforced in Germany. The Code of Civil Procedure also provided that, whilst an arbitral award had the effect of a final judgment, the same could not be enforced without an enforcement order made by a court and that the court would not make such an order if grounds existed for setting the award aside. No such order had been made in relation to the award in question, which Eve J described as "still-born" until a court "breathed life" into it. [38]

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36 op cit, at 106.
37 op cit, at 105.
38 op cit, at 105-106.

When that happened, the award was:-

> " . . . endowed with one, at least, of the essential characteristics of a judgment - the right to enforce obedience to it." [39]

Had the relevant order been made in Germany, it seems that Eve J would have permitted enforcement.

Eve J made only passing reference to the fact that the parties had agreed to arbitrate. His Honour did not canvass whether the underlying contractual regime might have provided the basis for enforcement - ie, by agreeing to go to arbitration, the parties had impliedly agreed to observe the requirements of any award arising from such arbitration. His Honour seemed to be suggesting that the right to require obedience to the award rested on whether the award carried the authority of a judgment. In other words, the implied contractual undertaking to abide by an award did not seem to be relevant - it was necessary to find instead some command mechanism and His Honour looked to the authority of the courts in rendering judgments. [40]

His Honour's approach has been the subject of some criticism. Lorenzen states that the process involved before the courts in Germany was no more than the equivalent of the requirement under England law for leave to enforce an award. [41] The requirement under the German Code of Civil Procedure was purely for the purposes of the local (ie, within Germany) enforcement of the award. As enforcement of the award was not being sought in Germany, however, this requirement should have been irrelevant, as far as the Court of Chancery was concerned.

The author says:-

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39 ibid.

40 As His Honour said, the only point was whether the Courts of the United Kingdom ought to recognise the award as a "foreign judgment".

41 Lorenzen, op cit, at 52.

> "The order of enforcement . . . is no more than the simple English decree for leave to enforce an award and does not transform the award into a judgment any more than does the English leave to enforce." [42]

Consequently, Eve J in the High Court, after finding that the award was "valid and binding" [43] should then have granted leave to enforce, as no further consideration was warranted. Nothing remained to be done other than to grant leave. In other words, even if the parties' contractual agreement to arbitrate was not a relevant factor, the command mechanism His Honour was looking for had been satisfied in any event.

A short while after the decision in *Merrifield Ziegler,* the case of *Norske Atlas Insurance Co Limited v London General Insurance Co Limited* [44] was heard before MacKinnon J in King's Bench division. The plaintiffs (a Norwegian company) had entered into a contract of reinsurance with the defendants, who were based in London. The contract, which provided that in the event of a dispute, an arbitration should take place in Norway, was valid under the law of Norway, but not that of England. An arbitration was held in Norway, with the award being given in favour of the plaintiffs. The plaintiffs sought to enforce the award in the English Courts. The defendants resisted, arguing that, as they resided in England, an award against them could only be enforced by the English courts. That being the case, the law applicable to the whole contract was that of England. Counsel for the defendants relied on authorities where reinsurance contracts had not been enforced, due to failure to meet the requirements of English law.

MacKinnon J rejected these arguments. His Honour said that had the plaintiffs been suing on the contract, then the defences raised may well have succeeded. The plaintiffs, however, were not suing on the contract, but rather, the award. All that the plaintiffs had to establish were:-

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42 At 54.
43 See the judgment of Eve J at 105.
44 (1927) 43 TLR 541.

" . . . (1) the submission; (2) the conduct of the arbitration in accordance with the submission; and (3) the fact that the award was valid according to the law of the country where it was made." [45]

His Honour said that as none of these issues were contested, the award was "perfectly good" and the plaintiffs were entitled to recover. [46]

There is no reference in the report to whether His Honour considered whether the award had to be "final", or "final and binding". The award was issued on 14 April the plaintiffs commenced their action in the Court of King's Bench shortly afterwards on 18 May 1926. No reference is made as to whether time for leave to appeal to a court in Norway had run out, or whether some other process was available to the defendants. MacKinnon J was satisfied that the award was valid and accordingly, it could be enforced. Perhaps the defendants were precluded (at least tactically) from raising such points by insisting that the applicable law of the contract was the law of England and, seemingly, not pleading in the alternative.

It seems clear, however, that the defendants were obliged to abide by their contractual undertaking to arbitrate and to consequently observe the provisions of any award. [47]

The focus in both *Merrifield Ziegler* and *Norske Atlas* was on the award. In the latter case, the fact that the original contract was unenforceable in England was not considered an impediment to enforcement. In the later decision of *Bremer Oeltransport GmbH v Drewry* [48], the question arose as to what it was that was being enforced - the award, or the contract between the parties. The plaintiff, a German firm, had sought enforcement of an award made in its favour in Hamburg, following arbitration there. The contract between the parties (a charterparty, which also contained the arbitration agreement) had been made in London.

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45 at 542.

46 ibid.

47 It is believed that this case was the first successful enforcement of a foreign award at common law in the United Kingdom - Dicey and Morris, *Conflict of Laws*, 11th edition, Stevens & Sons, 1987, at 561.

48 [1933] 1 KB 753.

The arbitrator had determined that the defendants should pay the plaintiffs a certain sum of money. As the amount of the award was not paid, the plaintiff obtained *ex parte* a court order in England, under which they were entitled to apply for the issue of a writ against the defendant (who resided in Paris). They so applied and, in the writ, sought payment of the moneys awarded by the arbitrator.

The plaintiffs were given leave to serve the writ outside the jurisdiction and the defendant then sought to have the order set aside. Slesser LJ in the Court of Appeal (with whom Romer LJ agreed), noted the decision in *Norske Atlas* and that MacKinnon LJ had treated the action as one upon the award, not on the parties' contract. [49]

Slesser LJ stated:-

> "The rights of the parties in respect of specific performance are the same as if the award had simply been an agreement between them." [50]

Counsel for the appellant referred to old authorities, some of which were based on actions to enforce penalty provisions in bonds. The approach of the earlier courts had been to distinguish between actions on an award and those on a bond; with the former, the plaintiff had to establish mutual submission to arbitration, but with the latter, the onus shifted to the defendant to prove that the conditions of the bond had been met. Consequently, the plaintiff had a greater onus if suing on an award, than if on a bond. Counsel submitted that the appellant's action was analogous to suing on a bond. Slesser LJ disagreed, stating that the greater weight of opinion favoured the approach that an action on an award:-

> " . . . is really founded on the agreement to submit the difference of which the award is the result . . . it is sufficient for the . . . plaintiffs to show that they are suing on the charter party made in London and more particularly on the submission to arbitration therein contained." [51]

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49 op cit, at 761.
50 *Bremer Oeltransport*, op cit, at 760.
51 op cit, at 764.

In other words, the award was but the manifestation of the parties' agreement. The Court was enforcing the parties' original agreement. Slesser LJ left open the question whether an action would lie "on an implied contract in the award itself" and held that the plaintiffs could commence proceedings based on their agreement to refer disputes. In this context, the proceedings were:-

> " . . . an action for the enforcement of a contract made within the jurisdiction." [52]

In the United States, the focus was on the award and whether that *per se* could be challenged. Domke says that, in relation to domestic awards in the United States, validity depended upon the law of the place of rendition of the award. [53]

The author refers to two cases where the same principle was applied to foreign awards. [54]

The first of these is *Gilbert v Burnstine et al* [55], in which the defendants had contracted for the supply of chemicals, but had subsequently refused to pay. Under the arbitration clause in the contract, the parties had agreed to arbitrate "all differences" under the contract in London, under England law.

The suppliers served notice requesting that the defendants concur in the appointment of an arbitrator. The defendants did not respond and the suppliers served a summons (issued out of the Court of King's Bench in London) on the defendants, seeking orders that the Court appoint an arbitrator. Again, there was no response from the defendants and the Court appointed an arbitrator in their absence. There was still no response when the arbitrator served notice on the defendants requiring production of all relevant documents. The arbitration proceeded *ex parte*, with an award made against the defendants, which the suppliers sought to enforce in New York. The

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52 op cit, at 765.

53 Domke, "Enforcement of Foreign Arbitral Awards in the United States", in 13 *Arbitration Journal* (1958), 91, at 92.

54 op cit, at 93 *et seq.*

defendants resisted on a number of grounds, including denying that they had ever agreed to submit to arbitration and that the arbitration agreement was, in any event, contrary to public policy.

The Court of Appeals of New York firstly stated that settlements of disputes by arbitration:-

> " . . . are no longer deemed contrary to our public policy. Indeed, our statute encourages them." [56]

O'Brien J (with whom the remainder of the Court agreed) noted that it was not against public policy for parties to agree in advance to be subject to a foreign jurisdiction. His Honour continued that contracts made by "mature men who are not wards of the court" ought to be enforced, in the absence of "potent objection":-

> "Unless individuals run foul of constitutions, statutes, decisions or the rules of public morality, why should they not be allowed to contract as they please?" [57]

The Court held that the defendants, after agreeing to arbitration, but then deciding to stay away from the arbitral hearing, could not dispute that they were bound by an award made after "due compliance" with the agreed procedures. [58]

In *Sargant v Monroe* [59], the parties had submitted to arbitration in London. The defendant appeared via an agent. The arbitrators found in favour of the plaintiffs. The agent then requested that the arbitrators state a number of points of law in the form of a special case for consideration by the courts.

Porter J, in the Court of King's Bench, declared that the award was correctly decided and entered judgment in favour of the plaintiffs.

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55 255 NY 348 (Court of Appeals, NY, January 13, 1931).
56 op cit, at 353.
57 op cit, at 354-355.
58 op cit, at 358.

The plaintiffs then brought an action in the Supreme Court of New York, on two grounds - the first, seeking enforcement of the orders of Porter J and the second on the award itself. The Appeals Court held that the orders (of the Court of Kings Bench) could not be enforced. The judgment could not be relied on, as it had been entered at the request of the agent and this was beyond the scope of his authority. On the other hand, the award could be enforced (and judgment entered thereon), as the agent had authority to act in respect of the arbitration. Glennon J, who delivered the unanimous verdict of the court, said:-

> "The parties submitted to arbitration, selected their own arbitrators, impliedly agreed to abide by their decision and participated in the arbitration which proceeded to a final award, in accordance with the procedure requested by the defendant . . . The defendant, therefore, cannot be heard to impeach the finding of the arbitrators." [60]

The courts accordingly held parties to their agreements to arbitrate.

Sargant v Monroe might be contrasted with the approach taken by Slesser LJ in *Bremer Oeltransport GmbH v Drewry*. [61] Whilst His Lordship left open the question of whether an action could be founded on an implied contract in the award, the New York Court of Appeals focused on the award itself – given the agreement to arbitrate, the award, if properly made, could not "be impeached". Further, there was an implied agreement to abide by the terms of any award.

Bremer Oeltransport was considered in *F J Bloemen Pty Limited v City of Gold Coast Council.* [62] An award made in Queensland for a sum of damages favoured the appellants. The respondents paid the amount of the award. The original agreement had provided for the payment of interest on amounts overdue. After the payment of the amount of the award, the appellants issued a writ, seeking payment from the respondents of interest under the original provisions. The Supreme Court of

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59 49 New York Supplement, 2d Series, 546 (Supreme Court of New York, June 28, 1944).
60 op cit, at 548.
61 op cit.
62 [1973] AC 115.

Queensland dismissed the claim, holding that holding that the award had superseded the rights under the contract.

The Privy Council dismissed the appeal. Their Lordships said that an award could not be viewed in isolation from the submission to arbitration. Whilst a fresh cause of action did arise from an award, superseding that which arose on breach of the original contract, it did not follow that the new cause of action based on the award could not be said to have arisen from the original contract. This was the "sort of consideration" which led the Court of Appeal to hold as they did in *Bremer Oeltransport*. [63]

Bremer Oeltransport was also considered in *Agromet Motoimport v Maulden Engineering Co (Beds.) Limited.* [64] Otton J accepted the submissions of counsel for the plaintiff, who had argued that the parties' original agreement was not being enforced, as a new and independent cause of action flowed from the award. Whilst it was an implied term of the original agreement that awards would be observed, the award itself was distinct from "and not entangled with" the original agreement. The authority of *Bremer Oeltransport* was really concerned with procedural issues. The central issue in that case was that the plaintiffs were attempting to satisfy the Court that their contract fell under the jurisdiction of the English Courts. [65]

B. Early Conventions

Geneva Protocol and Geneva Convention

As States claimed sovereignty and established individual legal systems, conventions grew into use as the importance of international relationships grew:-

> "There are two possible ways in which this lack of unanimity among the various systems of Private International Law may be ameliorated. The first is to secure by international conventions the unification of the internal laws of the various countries upon as many legal topics as possible." [66]

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63 op cit, at 126.
64 [1985] 1 WLR 762.
65 op cit, at 772.
66 Chesire, *Private International Law*, Third Edition, Clarendon Press, 1947.

As noted above in this Chapter, the United States and England had, via the Jay Treaty, undertaken to honour the arbitral awards of the various Commissions established for the purposes of the treaty. One shortcoming with bilateral relations, however, is that the recognition and enforcement of awards can only be established on a piecemeal basis.

Quigley provides a brief overview of the United States' attempts to provide for commercial arbitration regimes and the enforcement of awards in its bilateral treaties. The author notes that rather than contributing to the development of an "international" approach to commercial arbitration, the bilateral treaty regime, for the most part, merely embedded the existing law of the two countries involved. [67]

International trade grew enormously in the twentieth century and a large part of world trade is carried out by trade associations utilising standard contract conditions. [68] Such contracts mostly call for arbitration in the resolution of disputes, under either the rules of the relevant trade association, or an institution such as the ICC. Arbitration is considered preferable to proceeding via litigation, as it avoids:-

> " . . . the diversity of national laws, the complexities and delays of a lawsuit in a foreign court and the lack of expertise of most judges in most matters involving international commerce . . ." [69]

During the 1920s, the League of Nations, with its primary object being the maintenance of peace and its concern with high politics, had started to come under pressure from international business to intervene in private relations, to "foster the reconstitution of a *jus gentium*." [70]

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67 Quigley, "Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards", *The Yale Law Journal*, Volume 70, 1961, at 1049.

68 Berman and Kaufman, "The Law of International Commercial Transactions (*Lex Mercatoria*)", *Harvard International Law Review*, Volume 19, 1978, 221, at 228.

69 ibid.

70 David, op cit, at 143. There is some debate as to precisely what role the *jus gentium* fulfilled. Goldman, in *Lex Mercatoria*, Forum Internationale, 1983, at 3, quotes Francesakis as describing the *ius gentium* as coming about by the reception into Roman Law of "an *international custom of commercial law.*" (original emphasis). De Ly states that whilst the *ius*

One of the responses promoted by the League relating to arbitration was in the form of the Geneva Protocol on Arbitration Clauses ("Geneva Protocol"). The Geneva Protocol was opened at the Assembly of the League of Nations on 24 September 1923. It provided that Contracting States were to recognise the validity of arbitration clauses, whether or not the arbitration was to take place in a country to whose jurisdiction none of the parties in the arbitration was subject. [71]

Whilst many countries already recognised the validity of arbitration clauses, David continues, it was hoped that the Geneva Protocol would lead to more States recognising arbitration clauses and to "banish doubts" over the validity of such clauses. Further, the Geneva Protocol was a classic conception of international law. It did not seek to create rules of general application; rather, it ameliorated rules which might apply to the parties within the various Contracting States. [72]

The Geneva Protocol also made provision for the recognition and enforcement of arbitral awards in the territory of the State in which they were made - Article 3.

As the Geneva Protocol was somewhat limited in its scope, something additional was needed. On 26 September 1927, the Convention on the Execution of Foreign Arbitral Awards ("Geneva Convention of 1927") was opened. It is worth considering some of the detail of the Geneva Convention of 1927 (particularly in relation to recognition and enforcement), as many of the provisions survived to be included in the New York Convention (which has now largely supplanted the Geneva Convention).

Article 1 provides that, in the territory of any Contracting State, an arbitral award made in pursuance of an agreement covered by the Geneva Protocol, is to be recognised as binding and is to be enforced in accordance with the procedure of the

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gentium was part of Roman Law, it is not clear whether it was applied only between foreigners and between Romans and foreigners, or whether also in relations purely between Roman citizens as well. De Ly also states that there is debate over the sources of the *ius gentium* and whether it formed an autonomous legal system, distinct from Roman Law - De Ly, *International Business Law*, Elsevier, 1992, at 8, *et seq*. It is perhaps in the sense of the *ius gentium* as understood by Francesakis that David makes his comment.

71 Article 1 of the Geneva Protocol.

72 David, op cit, at 143.

territory where the award is relied upon. In order to obtain such recognition or enforcement, Article 1 also provides that it is necessary that:-

- the award must have been made in pursuance of a submission which was valid under the applicable law;

- the subject matter of the award must be capable of settlement by arbitration in the country where it was sought to enforce the award;

- the arbitral tribunal which made the award must have been the tribunal provided for in the submission, or constituted in the manner agreed by the parties and in accordance with the law governing the procedure;

- the award had become final in the country in which it was made and was not the subject of further proceedings in that country;

- the recognition of the award was not to be contrary to the *public policy* or the principles of law of the country in which it was sought to be enforced.

Article 2 provides that, even if the conditions in Article 1 are fulfilled, recognition and enforcement shall be refused if:-

- the award has been annulled in the country in which it was made;

- the party against whom enforcement is sought was not given sufficient notice of the proceedings, or, being under a legal incapacity, was not properly represented;

- the award does not deal with the differences contemplated by the parties, or it contains decisions on matters beyond the scope of the submission.

Article 3 provides that if the party against whom an award has been made establishes that there are grounds (with certain exceptions) which entitle that party to contest the validity of the award, then a Court, if it thought fit, could either refuse recognition or

enforcement, or adjourn any consideration thereof, to give the party a reasonable time to apply to have the award annulled.

Problems with the Geneva Protocol and Geneva Convention

The procedures under the Geneva Convention were seen as having certain drawbacks, however. Van den Berg refers to some of them - firstly, parties had to be subject to the jurisdiction of a Contracting State and the award had to have been made in a Contracting State. [73]

Further, there was the requirement that the award be "final" in the country where it had been made. This was widely interpreted as requiring the successful party obtaining leave to enforce in both the country where the award was made and the country in which it was sought to be enforced. This was known as the "double exequatur."

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[73] Van den Berg, Albert Jan, *The New York Convention: Towards a Uniform Judicial Interpretation*, Kluwer, 1981, at 7.

CHAPTER II

THE NEW YORK CONVENTION AND THE UNCITRAL MODEL LAW

> *". . . one of the most important features of an award in international commercial arbitration is that it should be readily transportable. It must be capable of being taken from the state in which it was made, under one system of law, to other states in which it is able to qualify for recognition and enforcement, under systems of law."* [1]

Background

The Second World War delayed any initiatives for improving the operation of the Geneva treaties (the Geneva Protocol of 1923 and the Geneva Convention of 1927). [2]

In the early 1950s, the ICC promoted a new international regime. A Draft Convention was published in 1953, which referred to what were described as "international" awards. The ICC proposals would have "delocalised" (or "internationalised") awards. The idea was to provide for an arbitration:-

> ". . . which would not be governed by a national law." [3]

The new proposals were not acceptable to the majority of States, however, who wished to retain supervision:-

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1 Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, Third Edition, Sweet & Maxwell, 1999, at paragraph 10-18.454

2 Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, Second Edition, Sweet & Maxwell, 1991, at 477.

3 Van den Berg, op cit, at 7.

> "Most States could not accept that the powers of national courts should be enlisted to enforce an award where the arbitrations concerned had not been governed by a national system of law." [4]

The ICC requested ECOSOC to convene an international conference to discuss the proposals. ECOSOC duly convened the conference, producing its own draft convention, which referred to "foreign" awards, rather than the "international" awards of the ICC proposal. The conference was held in New York in May and June of 1958 and became commonly known as the New York Conference of 1958. During its course, the delegates negotiated and settled the terms of the New York Convention.

Why is the New York Convention so important?

As van den Berg states:-

> " . . . the New York Convention can be considered as . . . the cornerstone of international commercial arbitration." [5]

Recently, on the fortieth anniversary of the New York Convention, delegates assembled at the UN in New York to mark the occasion. In a speech to the Assembly, the Argentine ambassador said:-

> "Unless it is ensured that foreign arbitral awards . . . can be recognised and enforced . . . a State places its traders and enterprises at a clear competitive disadvantage . . .
>
> The modern State can then be seen to have an inescapable responsibility - or rather an essential need - to provide its private sector with the necessary instrumental framework to enable it to compete with its foreign counterparts

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[4] Redfern and Hunter, Second Edition, op cit, at 478.

> without being disadvantaged. The State is required to play a pro-active role in this respect.
>
> The New York Convention . . . represents . . . an essential tool for competing in the increasingly liberalized environment of international trade between private individuals. It is, therefore, nothing less than a necessity." [6]

There are a number of important statements here. Cardenas states that each State has an obligation to ensure that its citizens are able to compete internationally; because of this, the State *must* become a party to regimes such as the Convention. Cardenas also sees that the Convention is essential for the workings of an increasingly liberal trade regime.

Main Provisions of the New York Convention relating to the recognition and enforcement of awards

Countries adopting the Convention are referred to as Contracting States. The Convention contains 16 Articles.

Article 1

Article 1.1 provides that the Convention shall apply to the recognition and enforcement of arbitral awards made in a jurisdiction other than that where it was sought to have the award recognised and enforced. The Convention also is to apply to awards which are not considered as "domestic" in the State where recognition and enforcement are sought.

Further, awards must arise out of "differences" between parties.

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5 van den Berg, op cit, at 1.

6 Cardenas, "Benefits of Membership", *Enforcing Arbitration Awards under the New York Convention*, UN Publication E.99.V.2 1999.

Article 1.2 provides that the Convention recognises "arbitral awards" as including those made by arbitrators appointed for each case, as well as those made by permanent arbitral bodies to whom the parties have submitted.

Under Article 1.3, Contracting States, when adopting the Convention, may, on the basis of reciprocity declare that they will apply the Convention only to the recognition and enforcement of awards made in the territories of other Contracting States (the "first reservation") and they may also declare that they will apply the Convention to differences arising out of legal relationships which are defined as "commercial", whether based on contract or not (the "second reservation").

Article II

In Article II, Contracting States agree to recognise arbitration agreements in writing under which parties have agreed to submit to arbitration all or any differences between them, arising out of a defined legal relationship, whether contractual or otherwise, concerning a matter capable of settlement by arbitration. The requirement of writing can be met by including an arbitration clause in a contract, or by the exchange of letters or telegrams.

Articles III, IV and V

The major provisions relating to the recognition and enforcement of arbitral awards are found in Articles III, IV and V.

Firstly, the difference between recognition and enforcement might be noted. These are quite separate concepts; recognition, on its own, is a defensive process, whilst enforcement (which must be preceded by recognition) goes one step further. [7] On occasions, the party against whom the award has been made, will look for grounds on which to attempt to persuade a court to deny recognition. In such cases, recognition alone is the issue. On the other hand, the party in whose favour the award was made,

will not only seek recognition, but, following that, enforcement. The authors note that the choice of wording in the Geneva Convention of 1927 was "more precise" than the Convention, in that it spoke of "recognition *or* enforcement" of awards (original emphasis). [8]

Article III of the Convention provides that Contracting States shall recognise arbitral awards as binding and shall enforce them in accordance with the rules of procedure in the territory where the award is relied on, under the conditions laid down in the Convention. Article III provides further that there shall not be imposed "substantially" more onerous conditions, or higher fees and charges on the recognition and enforcement of awards to which the Convention applies, than those which apply to domestic awards.

Article IV states that to obtain recognition and enforcement, the applicant must produce the "duly authenticated" original award, or a "duly certified" copy thereof, together with the original arbitration agreement, or a duly certified copy thereof.

Article V sets out the grounds on which the recognition and enforcement of an award may be resisted. The grounds are exclusive - the main points being:-

- where the parties are under some incapacity, or the arbitration agreement is invalid;

- the defendant was not given proper notice of the appointment of the arbitrator, or the proceedings, or was otherwise unable to present his or her case;

- the award deals with differences not contemplated by the reference, or beyond the scope of the reference;

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[7] Redfern and Hunter, Third Edition, op cit, at paragraphs 10-10 to 10-12.

- the composition of the arbitral authority or the arbitral procedure was not in accordance with the relevant law; and

- the award has not yet become binding, or has been set aside under the law of the country in which it was made.

Public policy under the New York Convention

Article V also provides that recognition and enforcement may be refused if a competent authority in the country in which the award is sought to be enforced determines that:-

- the subject matter of the dispute is not capable of settlement by arbitration under the law of that country; or

- recognition or enforcement of the award would be contrary to the *public policy* of that country.

UNCITRAL Model Law

The New York Convention, whilst a landmark, was seen as having one significant drawback – it relates primarily to agreements and awards, not the conduct of arbitral proceedings themselves:-

> ". . . the limited scope of the Convention prevented it from stipulating detailed provisions for the conduct of arbitration proceedings . . . To ameliorate this problem, the Model Law was designed to establish a uniform legal framework for the fair and efficient conduct of arbitration proceedings." [9]

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[8] Redfern and Hunter, op cit, at paragraph 10-09.

Redfern and Hunter note that the UNCITRAL [10] Model Law arose out of a request in 1977 from the Asian-African Legal Consultative Committee for a review of the New York Convention. [11] The authors state that there was some concern over an apparent "lack of uniformity" shown by national courts in enforcing awards, which led to the then Secretary-General of UNCITRAL preparing a report which recommended the adoption of a uniform arbitration law. [12]

This is UNCITRAL's advance on the New York Convention - the Model Law (*inter alia*) introduced provisions for the conduct of arbitrations. The Model Law is a *lex specialis*, intended to apply "to the exclusion of all other pertinent provisions of non-treaty law." [13]

Article 1 provides that the Law applies to "international commercial arbitration", subject to any agreement in force between the adopting State and other States. The expression "commercial" is to be given a wide interpretation, as it is intended to cover matters arising from "all relationships of a commercial nature, whether contractual or not." Article 1(3) also provides that arbitration is "international" if:-

- the parties have their place of business in different States; or

- one the following places is located outside the State in which the parties have their places of business:

  (i) the place of arbitration; or

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9 Chukwumerije, *Choice of Law in International Commercial Arbitration*, Quorum Books, 1994, at 98.

10 By Resolution 2205(xxi), dated 17 December 1966, the United Nations General Assembly established UNCITRAL, whose principal object is to harmonise and unify the law of international trade.

11 Redfern and Hunter, Second Edition, op cit, at 508.

12 ibid. That report is UN Document A/CN.9/264, 25 March 1985 - *Analytical Commentary On Draft Text of a Model Law in International Commercial Arbitration.*

(ii) any place where a substantial part of the obligations under the commercial relationship between the parties is to be performed, or the place with which the subject-matter of the dispute is most closely connected; or

the parties have agreed that the subject matter of the dispute relates to more than one country.

Article 28(1) provides that the arbitral tribunal shall decide the dispute in accordance with such legal rules as are chosen by the parties. Where the parties designate the law of a particular State, this shall be taken as nominating the substantive law of that State and not to its conflicts rules. Where the parties do not designate any system of law, the arbitral tribunal shall apply the law determined by the conflicts rules which it considers appropriate – Art 28(2). The tribunal may only decide *ex aequo et bono* or as *amiable compositeurs* where expressly authorised by the parties to do so – Art 28(3). The tribunal shall, in all cases, decide in accordance with the terms of the contract and must also take into account relevant trade usages – Art 28(4).

Article 35 provides that awards shall be recognised as binding and shall be enforced in accordance with Article 36.

Public policy under the Model Law

Public policy is referred to in Articles 34 and 36. Article 34 provides a regime for directly attacking an award in the jurisdiction in which it was made. The New York Convention recognises that awards may be set aside by courts and makes provision for both where an application has been made, and where a court has actually ordered the setting aside – Articles V.I(e) and VI. The Convention is otherwise silent on applications for setting aside awards. Obviously, as arbitration laws vary from

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[13] Report of the Secretary-General, op cit, at 35.0-7.

jurisdiction to jurisdiction, there was a "great variety of ways" in which awards could be attacked under national laws. The Secretariat [14] suggested, accordingly, that:-

> " . . . the Model Law should stipulate a single, exclusive method of judicial recourse against the award . . . ". [15]

Grounds for setting aside awards

Article 34(2) sets out an exhaustive list of grounds on which applications may be made to set aside awards. Briefly, these are:-

- where the parties were under some incapacity, or the arbitration agreement is invalid;

- the party making the application was not given proper notice of the proceedings, or was unable to present its case;

- the award deals with a dispute not falling within the terms of the reference;

- the composition of the tribunal or the procedure was not in accordance with the agreement of the parties;

- the subject matter is non-arbitrable; or

- the award is in conflict with the laws of the State whose courts are addressed.

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[14] The International Trade Law Branch of the UN Office of Legal Affairs acts as the Secretariat to UNCITRAL. Its role in the development of the Model Law was, *inter alia*, to prepare background reports and suggest draft texts - see Holtzmann and Neuhaus, *A Guide to the UNCITRAL Model Law in International Commercial Arbitration*, Kluwer, 1989, at 5.

[15] Holtzmann and Neuhaus, op cit, at 912.

There is a time limit for making the appeal of three months from the time of receiving the award.

Grounds for refusal of recognition and enforcement of awards

There is an intentional symmetry between Articles 34 and 36. The latter sets out the grounds on which a party may resist proceedings for the recognition and enforcement of an award. One question which arose during the drafting of the Model Law was the relationship between these two Articles - the problem of "double control" was discussed. This involved the possibility that different courts could be reviewing the same award on the same grounds. - ie, one under the setting aside provisions and the other looking at whether the award ought to be enforced. The Secretariat suggested that Article 36(2) could be utilised to avoid the problem - this Article provides that where an application to set aside or suspend the award has been made, the court where recognition or enforcement is sought may adjourn its decision. [16]

As noted, Article 36 closely follows Article 34 - the specified grounds in Article 36(1)(a) relate to incapacity, lack of notice (and inability to present a case); that the award deals with some matter not within the terms of the submission; that the arbitral tribunal was not properly composed, or the award has not become binding, or has been set aside or suspended by a court in which, under the law of which, it was made.

Art 36(1)(b) also provides further grounds:-

- lack of arbitrability; and

- where public policy would be offended.

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16 Holtzmann and Neuhaus, op cit, at 1062-1063.

The Secretary-General's Report also noted that, in relation to foreign awards, "full harmony" with the New York Convention "is obviously desirable." [17] It will of course, be noted that Article 36 is drafted in substantially similar terms to Article V.

The intention of the drafters clearly was to ensure that arbitration awards are to be handled under the Model Law in essentially the same way as under the New York Convention. It must, therefore, be expected that the case law in the area of the enforcement of awards under the Model Law would follow the existing case law under the New York Convention.

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[17] op cit, at 35.0-78.

CHAPTER III

THE ADOPTION OF THE NEW YORK CONVENTION AND UNCITRAL MODEL LAW - SOME BACKGROUND ISSUES RELATING TO THE SCOPE OF THE NEW YORK CONVENTION

"For the most part . . . international commercial arbitration depends for its full effectiveness upon the support of different systems of law . . . " [1]

A. Adoption of the New York Convention

The New York Convention is, classically, an instrument of Private International Law.

International conventions have been used to unify the rules of Private International Law. [2] States which have adopted the New York Convention are consequently relying on municipal law in recognising and enforcing awards. Some States (eg, Switzerland) have merely provided that issues concerning foreign awards are to be governed by the Convention; other States (eg, Australia) have repeated the terms of the Convention (sometimes with modifications) in their internal laws.

United Kingdom

After the early international regimes came into operation, the United Kingdom adopted them into legislation. With the Geneva Protocol, Parliament enacted *The Arbitration Clauses (Geneva Protocol) Act*, 1924 and after executing the Geneva Convention, it enacted *The Arbitration (Foreign Awards) Act*, 1930 (the "1930 Act").

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1 Redfern and Hunter, Third Edition, op cit, at paragraph 1-111.

2 For a discussion on the differences of approach between English and United States law in relation to Private International law, see Posner, *Law and Legal Theory in England and*

The 1930 Act incorporated both the Geneva Protocol and the Geneva Convention.

In 1950, Parliament consolidated, without amendment, the *Arbitration Act*, 1889, the *Arbitration Clauses (Geneva Protocol) Act*, 1924, the *Arbitration (Foreign Awards) Act*, 1930 and the *Arbitration Act*, 1934, into the *Arbitration Act*, 1950 (the "1950 Act").

Part II of the 1950 Act was headed "Enforcement of Certain Foreign Awards". S35 provided that Part II applied to any award made after 28 July, 1924, if made:-

- pursuant to an arbitration agreement to which the Geneva Protocol applied; and

- between persons one of whom was subject to the jurisdiction of England and the other of a territory who was a party to the 1927 Convention; and

- in a territory to which the Convention applied.

S36 provided that a foreign award "shall" be enforceable in England either by action or in the same manner as an award was enforceable under s26 of the 1950 Act; the latter section provided that awards may, subject to the leave of the High Court, be enforced in the same manner as a judgment or order to the same effect. [3]

S37(1) of the 1950 Act set out pre-conditions for enforcement. The award must have:-

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America, Oxford, Clarendon Press, 1996.

[3] In *Dalmia Cement Limited v National Bank of Pakistan*, [1975] QB 9, Kerr J held that s26 of the 1950 Act could be directly invoked in relation to foreign awards which did not fall under Part II.

- been made in pursuance of a valid arbitration agreement; and

- been made by the tribunal agreed upon by the parties; and

- been made in accordance with the law governing the arbitration procedure;

- become final in the jurisdiction in which it was made; and

- been in respect of a matter which, under the law of England, was capable of being referred to arbitration.

S37(2) provided that an award should not be enforceable if the court dealing with the application was satisfied that the award had been annulled in the jurisdiction in which it was made; or the party against whom enforcement was sought was not given sufficient notice of the proceedings, or was under some legal incapacity and was not properly represented; or, the award did not deal with matters referred, or went beyond the scope of the arbitration.

For the purposes of Part II, s39 provided that an award should not be deemed "final" if any proceedings contesting the validity of the award were "pending" in the place of the making of the award.

S21 of the 1950 Act set out the "stated case" procedure, under which an arbitrator could (being required to do so if directed by the High Court) state a special case for the decision of the High Court on any question of law arising in the course of an arbitral reference or on an award. [4]

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[4] The "stated case" procedure was on one of the reasons why London lost some favour as an arbitral centre. This is discussed further in Chapter V.

The United Kingdom became a Contracting State under the New York Convention on 24 September 1975. The *Arbitration Act* 1975 (the "1975 Act") was enacted to provide for the enforcement of Convention awards. S3 provided that Convention awards "shall . . . be enforceable" in the same manner as an award of an arbitrator was enforceable by virtue of s26 of the 1950 Act. S5(1) provided that enforcement of a Convention award could only be refused on the grounds set out in that section – the grounds set out in the remaining provisions of s5 repeated Articles V.1 and V.2 of the Convention.

"Convention award" was defined to mean an award made in the territory of a State (other than the United Kingdom), which was a party to the Convention.

Then came the *Arbitration Act* 1979, which amended the provisions of the 1950 Act relating to appeals from awards. S1 of the 1979 Act repealed s21 of the 1950 Act which contained the stated case procedure.

More recently, the United Kingdom enacted the *Arbitration Act* 1996 (the "1996 Act"). The 1996 Act repealed *inter alia* the 1975 Act, the 1979 Act and Part 1 of the 1950 Act (which contained s26).

S99 of the 1996 Act provides that Part II of the *Arbitration Act* 1950 continues to apply to foreign awards (within the meaning of that Part) which are not also awards made under the Convention. The definition of "Convention Award" is the same as in the 1975 Act – that is, an award made in pursuance of an arbitration agreement, in the territory of a state (other than the United Kingdom), which is a party to the Convention.

S101 provides that a Convention award is binding upon the parties between whom it is made and may be enforced, by leave of the Court, in the same manner as a judgment or order of the Court to the same effect. S103 provides that recognition and

enforcement of a Convention award shall not be refused except as set out in s103, the remaining provisions of which repeat, as did the 1975 Act, Articles V.1 and V.2.

The position then seems to be that Convention awards (as defined) may be enforced under the 1996 Act; other foreign awards may be enforced under Part II of the 1950 Act (provided they meet the criteria set out there), whilst foreign awards not meeting either the criteria in either the 1996 Act or the 1950 Act, could be enforced under the common law, or s66 of the 1996 Act, which is in the same terms as s26 of the 1950 Act.

United States

The United States enacted its *Federal Arbitration Act* ("FAA") 1925, using as the model the *New York Arbitration Law*. Section 2 of FAA provided that written provisions in "maritime transactions" and contracts evidencing a transaction involving "commerce" (both of which expressions are defined in s1) agreeing to settle controversies by way of arbitration, shall be "valid, irrevocable and enforceable, save upon such grounds as exist in law or equity for the revocation of any contract". [5] S9 refers to enforcement by the Courts of arbitral awards.

The United States became a Contracting State under the New York Convention in 1970. Chapter 2 of 9 USC was enacted, to give effect to the provisions of the Convention. It came into force on 31 July 1970. 9 USC §201 provides that the New York Convention:-

> ". . . shall be enforced in United States Courts in accordance with this Chapter."

§202 provides that an arbitration agreement or arbitral award:-

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[5] Defined to include a range of transactions such as charter parties, bills of lading, etc and "any other matters" caught by the admiralty jurisdiction. "Commerce" was defined to include commerce between " . . . the several States or with foreign nations."

" . . . arising out of a legal relationship, whether contractual or not, which is considered as commercial . . . falls under the Convention."

Jurisdiction over actions concerning the Convention is given to the United States District Courts.

Switzerland

Switzerland is a confederation comprised of 26 cantons, each having its own legal code and court system. There is also a federal legal system. The Federal Constitution of 1874 provided that "questions of judicial organisation, procedure and the administration of justice remain within the competence of the Cantons".

Berger states that, historically, Swiss jurisprudence:-

". . . repeatedly emphasised the procedural nature of arbitration." [6]

This was reflected by the fact that, in 1915, the Federal Supreme Court ruled that arbitration agreements were governed, not by federal law, but by cantonal law on procedure. [7]

Switzerland became a Contracting State to the Convention on 1 June 1965, subject to the first reservation. On 23 April 1993, Switzerland withdrew its right to claim the first reservation.

In 1969, a number of cantons adopted the Intercantonal Arbitration Convention or *Concordat Suisse sur l'arbitrage* ("Concordat"), under which the participating cantons

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6 Berger, *International Economic Arbitration*, Kluwer, 1993, at 26.

7 Briner, National Reports (Switzerland), in *Yearbook Commercial Arbitration* XIV (1989) at 1.

agreed to unify their arbitration laws. By 1989, 25 of the 26 cantons had adopted the Concordat. [8]

Article 1 provides [9] that the Concordat's provisions are to apply to "any proceedings before an arbitral tribunal" the seat of which is located in a Canton, which is a party to the Concordat. It is also provided that the Concordat is not to affect the operation of institutional arbitration rules, so far as such rules do not offend against any of the mandatory provisions of the Concordat. Article 3 provides that the high court of civil jurisdiction of the Canton where the arbitration takes place shall be the competent judicial authority to, *inter alia*, give judgment in any action for the annulment or review of awards and the court may also declare the award enforceable.

Article 36 sets out the grounds on which a court may set aside an award. These include such matters as whether the arbitral tribunal was properly constituted, whether it erred as to its jurisdiction or violated due process and what has become a controversial ground, whether an award was "arbitrary". An award will be regarded as arbitrary, if it constitutes an "obvious violation" of law or equity.

The provisions of Article 36 may not be waived by the parties.

Another process available under the Concordat is that of review, under Article 41. This may occur if an award has been affected by fraud, or made without knowledge of significant facts which were unable to be adduced in evidence at the hearing. The primary difference between Articles 36 and 41 is that, under the former, the award may be set aside, whilst under the latter, the award is remitted to the arbitral tribunal for further hearing.

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8 ibid.

9 Text reproduced in Wetter, *The International Arbitral Process*, Volume IV, 1979. Oceana, at 387 *et seq.*

In more recent times, however, arbitration has been seen as having a contractual base. This, coupled with a pragmatic desire to make arbitration more "user-friendly", led to the enactment of federal legislation. In 1987, the *Loi federale sur le droit international privé* ("*Loi*") was enacted, Chapter 12 of which (containing Articles 176 to 194) deals with arbitrations.

Article 176 of the *Loi* provides that Chapter 12 applies to "international" arbitrations if the seat of arbitration is Switzerland and at least one of the parties has neither its domicile nor its "habitual residence" in Switzerland. The parties may, however, agree in writing to exclude the operation of Chapter 12 and that cantonal provisions on arbitration are to apply exclusively to their arrangements.

Under Article 190, with an international arbitration, there are certain (exclusive) grounds on which an award may be attacked - where the arbitrator was not properly appointed (or, in the case of a panel, not properly constituted); where the arbitrators wrongly accepted or declined jurisdiction; where the award went outside what was claimed, or did not decide a claim submitted; where the parties were not treated equally, or where the award is incompatible with public policy.

Under Article 192, if neither party is domiciled, nor has its habitual residence or place of business in Switzerland, the parties may waive the right to challenge an award, or they may exclude one or more of the grounds for challenge. If they so agree and it is sought to enforce a subsequent award in Switzerland, the provisions of the New York Convention apply "by analogy" - Article 192(2).

With "foreign" awards, Article 194 provides that these are governed by the New York Convention, irrespective of whether the State where the award is rendered is a "Convention" State. "Foreign award" is not defined, but it would seem that such an award would be one not otherwise coming under the *Loi*.

It would, therefore, seem that Switzerland has a number of regimes which could affect the arbitrations or enforcement actions of international parties. The Convention is applicable at one (possibly two) levels.

France

France adopted the Convention on 26 June 1959. It claimed the first reservation. Book IV of the *Nouveau Code de Procedure Civile* sets out the relevant provisions. This part of the Code was enacted in 1981. [10]

Article 1498 provides that awards shall be recognised and enforced in France so long as parties relying on them prove the existence of the award, and that they are not manifestly contrary to *international* public policy.

The decision to include "international" before "public policy" is unique. Kirry states that "international public policy" is synonymous with "mandatory rules of French law". [11]

Australia

Australia adopted the Convention with effect from 26 March 1975. It did so without adopting either reservation. The Convention was incorporated into the *Arbitration (Foreign Awards and Agreements) Act* 1974, the title of which was subsequently amended [12] to the *International Arbitration Act* 1974 ("the Act"). Sections 1-4 of the Act came into force on 9 December 1974 and the remainder on 24 June 1975.

Section 4 of the Act provides that "approval is given" for the accession by Australia to the Convention "without any declaration under sub-Article 3 of Article 1." [13]

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10 By the Decree of 12 May 1981 (*Décret n. 81-500 du 12 Mai 1981*).

11 Kirry, "Arbitrability: Current Trends in Europe", *Arbitration International*, 1996, Volume 12, No. 4, 373, at 385. International public policy is discussed further below, particularly in Chapters IV and XII.

12 By the *International Arbitration Amendment Act* 1989, No. 25.

13 The sub-Article relates to the permitted reservations.

Section 7(1) carries into effect the requirement under the Convention to afford recognition to arbitration agreements. It is provided that s7 applies to an arbitration agreement where:-

- the procedure relating to an arbitration under the agreement is governed (expressly or otherwise) by either the law of a Convention country, or a country not being Australia and one of the parties to the agreement is Australia, or a State, or a person ordinarily resident in Australia; or

- a party to the agreement is the government of either a Convention country, or part of such a country, or of a Territory (to which the Convention extends) of a Convention country; or

- a party to the agreement is ordinarily resident outside of Australia.

S7(2) has two aspects - it firstly provides that where a party to an arbitration agreement to which s7 applies has instituted legal proceedings in a court and those proceedings involve the determination of a matter that is, in pursuance of the agreement, capable of settlement by arbitration, then the court shall, on the application of any party to the arbitration agreement, stay the proceedings (conditionally, if the court sees fit). Sub-section (2) then provides that where a stay has been made, the Court shall refer the parties to arbitration. A party may consequently find that not only is its legal action stayed, but that it will be required to arbitrate.

Under s7(5), the court may not make any orders under s7(2) if it finds that the arbitration agreement is "null and void, inoperative, or incapable of being performed."

With regards to enforcement, s8(1) of the Act provides that a "foreign award" is binding, by virtue of the Act "for all purposes on the parties to the arbitration agreement in pursuance of which it was made." S8(2) provides that a foreign award may be enforced in a court of a State or Territory as if the award had been made in that State or Territory, in accordance with the law of that State or Territory. The various States and Territories within Australia have (for the most part) uniform *Commercial Arbitration Acts* [14], s 33 of which provides that awards may, by leave of the Court [15], be enforced in the same manner as a judgment or order of the Court to the same effect and where such leave is granted, judgment may be entered in terms of the award.

The grounds for the refusal of enforcement are set out in sub-section (5). The language used is largely that of Article V of the Convention. A significant difference is that Article V states that recognition and enforcement may be refused *only* if any of the grounds set out are established. In s8(5) of the Act, the word "only" is omitted.

A party seeking enforcement of a foreign award must also meet the requirements of s9. That party must produce to the Court the duly authenticated original award, or a duly certified copy, together with the original arbitration agreement (or a duly certified copy). S9(2) sets out what is required for "due authentication" of an award - where it has purportedly been authenticated or certified by the arbitrator (or officer of an arbitral tribunal) and it has not been established to the Court that the award has not been so authenticated or certified. S9(2)(b) provides that the Court may also be satisfied, if the award has been "otherwise" authenticated.

Where the award is in a language other than English, s9(3) requires that the translation be certified by a diplomatic or consular agent in Australia of the country in which the award was made, or "otherwise" to the satisfaction of the Court.

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14 In New South Wales, the *Commercial Arbitration Act*, 1984.

15 Which, in New South Wales, is the Supreme Court of New South Wales, or, where the parties have agreed, the District Court of New South Wales.

One other provision of note is s2C, which relates to the carriage of goods by sea.

In the Act as enacted in 1974, the original reference was to the *Sea-Carriage of Goods Act* 1924 ("the 1924 Act"); this has now been supplemented by reference to the *Carriage of Goods by Sea Act* 1991 ("the 1991 Act"). S9 of the 1924 Act provided that the parties to a bill of lading or document relating to the carriage of goods from any place in Australia to any place outside Australia shall be deemed to have contracted according to the laws in force at the place of shipment. Any agreement to the contrary, or one purporting to lessen or oust the jurisdiction of Australian courts in respect of the bill of lading or other document, was null and void. Section 9(2) also rendered null and void any agreement in respect of a bill of lading which purported to do likewise in respect of the carriage of goods from any place outside Australia, to any place within.

The 1991 Act repealed the 1924 Act and the then s2C of the *International Arbitration Act*. Section 20(2) of the 1991 Act provides for the continued operation of s9 of the 1924 Act for agreements made before the coming into effect of the 1991 Act.

Ss11(1) and 11(2) of the 1991 Act provided in similar terms to the old s9. S11 has been amended by the *Carriage of Goods by Sea Amendment Act* 1997, however. A new sub-section [sub-s11(3)] was added, which provides that an arbitration agreement is not made ineffective by s11(2) if the agreement provides that arbitration must be conducted in Australia.

B. Adoption of the UNCITRAL Model Law

Whilst Australia and Switzerland are signatories to the Model Law, the United Kingdom and the United States are not, although the United Kingdom has incorporated features of the Model Law into its *Arbitration Act*, 1996.

Australia

In Australia's *International Arbitration Act* 1974, s16 provides that the Model Law, subject to Part III of the Act, has "the force of law in Australia." S19 provides that, for the avoidance of doubt and without derogating from Article 34(2)(b)(ii) of the Model Law, an award is in conflict with the *public policy* of Australia if the making of the award was induced or affected by fraud or corruption, or a breach of the rules of natural justice occurred in connection with the making of the award.

This seems to have a narrow operation – the fraud or corruption must be connected to the making of the award itself.

C. Background issues associated with the New York Convention

Firstly, it is clear that the New York Convention has achieved a significant status. At present, more than 145 countries subscribe to it.

A uniform approach?

Probably the most significant factor which initially propelled the Convention to near universal acceptance was the idea that adoption would lead to much less uncertainty in the recognising and enforcing of arbitral awards. As noted, some of the major advances created by the New York Convention over the Geneva Convention included the reversal of the onus of proof and the abolition of the need for the award to be "final". Provisions such as these obviously narrowed the scope for resisting enforcement.

The New York Convention also reduced the ability of local courts to intervene in the enforcement process.

It has been suggested by some commentators (and courts) that municipal courts should move toward a uniform judicial interpretation of the Convention. In a decision of the New South Wales Court of Appeal, Kirby P (as he then was) said:-

> "It is highly desirable that, in the field of arbitration (both international and national), a common approach should be adopted by the Courts." [16]

What does the Convention cover?

As noted above, the draft Convention produced by ECOSOC referred to "foreign", rather than "international", awards. [17] David says this choice of expression was made for a "bad reason" - it was apparently felt by delegates that the expression "international award" should apply only in the sphere of public international law. [18]

Article 1.1 was drafted to include two limbs, firstly referring to awards made in the territory of a State other than the State in which recognition or enforcement is sought and, secondly, to awards which are "not considered as domestic awards" in the State in which recognition or enforcement is sought.

At the New York Conference of 1958, the final form of Article 1.1 came about as a result of a compromise between civil law and common law countries. Delegates from common law countries were in favour of a territorial test being applied to determine whether an award was "foreign" or "domestic". For example, the United Kingdom's legislation [19] required that in order to qualify as a "foreign award", an award must have been made:-

- pursuant to an arbitration agreement to which the Geneva Protocol applied; and

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16 *Ferris v Plaister* (1994) 34 NSWLR 474, at 491.
17 This was, of course, ultimately reflected in the formal title of the New York Convention.
18 David, op cit, at 147.
19 At that time, the *Arbitration Act*, 1950 (UK).

- between parties, one of whom was subject to the jurisdiction of a country with which the United Kingdom had made reciprocal arrangements under the Geneva Convention of 1927 and the other party being subject to the jurisdiction of another country to which the Geneva Convention of 1927 applied; and

- in a country to which the Geneva Convention of 1927 applied and with whom the United Kingdom had made the appropriate reciprocal arrangements. [20]

A "foreign award", therefore, had to have a territorial connection.

Civil law countries did not favour this approach, as, under their systems, the place of making the award was irrelevant towards determining whether an award was "foreign" or "domestic". For instance, under the then West German law, the status of an award was determined by ascertaining which law had governed the arbitral procedure. The West German delegate stated that the nationality of an arbitral award would then be derived from the rules of procedure and that:-

> ". . . it should be noted that those rules depended to a large extent, at least in German law, on the will of the parties . . ." [21]

The West German delegate said that the territorial criterion provided problems - as an example, two German parties might arbitrate in London, under German procedural law. If the "territorial" test was used, the award was English; however, under German law, as German procedural law had been applied, the award would be

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20 s35.

21 Reproduced in Gaja, *International Commercial Arbitration: The New York Convention*, Loose Leaf Collection, Dobbs Ferry, New York, 1978.

regarded as domestic. To hold that the award was English, would therefore, have the effect of infringing the will of the parties. [22]

In a speech supporting the West German position, the French delegate told the Conference that the place of the award was "often fortuitous or artificial" and sometimes, impossible to determine. [23]

The result was that the Conference compromised and adopted both criteria. Before examining what might constitute a "foreign" or a "non-domestic" award, however, some consideration might be given as to what might be regarded as an "award", ie, is every arbitral award an "award" for the purposes of the Convention?

What constitutes an "award" for the purposes of the Convention?

There was some discussion of this point in the United States decisions, *Spier v Calzaturificio Tecnica SpA* [24] and *Europcar Italia SpA v Maiellano Tours Inc.* [25] In both instances, the arbitration agreement had provided for arbitration in Italy and that the arbitral panel was to decide any controversy pursuant to the rules for "*Arbitrato Irrituale in Equita (procedimento informale)*" ("procedural arbitration" or "informal arbitration on equitable grounds").

In *Spier*, the defendant ("Tecnica") sought to resist enforcement of the award in the United States. Tecnica argued that *arbitrato irrituale* was not covered by the Convention, as it is an informal process, without "procedural safeguards". Such an arbitral process was to be distinguished from *arbitrato rituale*, awards arising from which are challengeable in the Italian courts only on very limited grounds. On the other hand, *arbitrato irrituale* was subject to a much wider range of defences under Italian law. Further, once in court, the matters were subjected to a *de novo* hearing.

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22 Gaja, op cit.
23 Gaja, op cit.
24 663 F. Supp. 871 (SDNY, 1987).

To support these arguments, Tecnica led evidence from a number of experts, including Professor Pieter Sanders. [26] Professor Sanders deposed that the Convention was intended to facilitate the enforcement of foreign arbitral awards "in the proper sense" [27] and, even though *arbitrato irrituale* had a contractual base, that the use of the word "binding" in the Convention was not intended to "open the door" to procedures which:-

> " . . . are not supported by the same statutory guarantees for proper proceedings as is the case for arbitration." [28]

Seemingly, *arbitrato irrituale* was not regarded as "proper" arbitration, or even as arbitration at all. Tecnica's Italian counsel, Professor Bernini also provided an affidavit, in which he distinguished between "procedural" and "contractual" arbitration.

Tecnica also pointed to a decision of the *Bundesgerichtshof* (Germany's highest court) which had held that the Convention did not cover such awards. At the same time Tecnica conceded that there were decisions of the *Corte de Cassazione* (the Italian Supreme Court) where the opposite conclusion has been reached.

The Court adjourned the proceedings, to allow Tecnica to approach the Italian courts for a review of the awards.

In *Europcar*, the Court of Appeals for the Second Circuit also noted the decisions of the *Corte de Cassazione* and said that that Court had recognised that these awards would be treated differently under the Convention than under Italian law.

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25 156 F.3d 310 (Second Circuit, 1998).

26 Described by the Court as "a principal draftsman" of the Convention.

27 op cit, at 874. It is assumed that the words "in the proper sense" were meant to qualify "awards", rather than "enforcement".

The Court of Appeals continued:-

> "Nevertheless, it (*the Corte de Cassazione*) held that in order to be enforceable under the Convention, awards must only be binding on the parties, not necessarily judicially binding in the originating country and that although awards under arbitrato irrituale are merely contractual and therefore are not merely enforceable in Italy, they are nevertheless binding on the parties." [29]

The Court did not have to decide the issue, but it noted that there were "compelling arguments on both sides". [30]

The answer to this difficulty must lie, it is suggested, in relying on the provisions of the Convention. If an award is contractually binding, then, *prima facie*, it is enforceable and one must look to see if any of the nominated defences apply. It is suggested that, so long as an award may be regarded as binding, reliance on the safeguards contained in the Convention would be preferable to the exercise of examining in detail the arbitral processes of other jurisdictions. If, for instance, the lack of procedural safeguards in *arbitrato irrituale* meant that the party resisting enforcement had been prevented from properly presenting its case, then the Convention provides a remedy against enforcement.

What is meant by "foreign" and "non-domestic" awards?

Putting aside any controversy as to whether any particular award may or may not be an "award" enforceable under the Convention, the scope of the first criterion of Article 1.1 seems readily ascertainable. Following the wishes of the common law delegates at the New York Conference, it applies on a "territorial" basis - where the

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28 ibid.
29 op cit, at 314.
30 ibid.

award has been made in a State which is not the State where recognition and enforcement might be sought. Further, Article 1.1 does not require that the State in which the award was made must be a Contracting State. (Contracting States, may however, choose to apply the Convention on the basis of the first of the permitted reservations, being that the recognition and enforcement of awards shall extend only to awards made in other Contracting States). [31]

Distinguishing which awards fall under the second "limb" has attracted some comment. In *Bergesen v Joseph Muller Corporation* [32], it was held that an award made in the State of New York was enforceable under the Convention in the United States. Neither of the parties were citizens of the United States. The plaintiff ("Bergesen") was a Norwegian shipowner; the defendant ("Muller"), a Swiss company.

Bergesen had initially attempted to enforce the award in Switzerland, but was unsuccessful. It then sought to have the award confirmed in New York, prior to the expiration of the limitation period (three years) specified in 9 USC §207. Muller argued that the award could not be a "foreign" award under the Convention, as it was made in New York. It then argued the award could not be "non-domestic"; this provision was inserted into the Convention to enforce what it termed "stateless" awards (generally, an award will be regarded as "stateless", if the arbitration is "detached" from State laws. More is said about this in Chapter XI).

Muller argued further that USC should be construed narrowly and further, USC (as far as it implemented the Convention) was not intended to cover awards made in the United States. The Court noted the provisions of 9 USC §202, which provide any award arising out of such a relationship which is entirely between citizens of the United States, will not fall under the Convention, unless that relationship:-

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31 The other reservation being the ability to apply the Convention only to matters which are considered "commercial" by the adopting State. This reservation was incorporated apparently at the request of countries such as Belgium, whose arbitration law is restricted to commercial matters only - Quigley, op cit, at 1061.

32 710 F.2nd 928 (Second Circuit, 1983).

> " . . . involves property located abroad, envisages performance or enforcement abroad, or has some other reasonable relation with one or more foreign states." [33]

The Court rejected each of Muller's propositions and referred to the deliberations of Congress on the implementation of the Convention. It was noted that Congress had stated that awards arising out of legal relationships between United States citizens could not be enforced under the Convention, unless there was a "reasonable relation with a foreign state." The Court noted that the framers of the Convention had apparently left it to each State to determine what constituted a "non-domestic" award and, further, that Congress had not specifically excluded awards involving two foreign parties rendered in the United States. [34]

Given this legislative background and the fact that the parties were not citizens of the United States, the Court decided that the award could be enforced under the Convention.

Van den Berg concludes that (for the purposes of the Convention) "non-domestic" awards can only be awards made *in* the State where recognition or enforcement is sought, but which have an "international" flavour. [35] States are free to establish whatever criteria they wish for the purposes of defining a "non-domestic" award. Quigley makes the same point, stating that the "non-domestic" criterion is not a limitation on the first limb of the scope of the application of the Convention (which he calls "the territorial test"); the conclusion must be that the non-domestic criterion applies to awards made within the State where enforcement is sought, but which are not considered as domestic by that State. [36]

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33 op cit, at 933.
34 ibid.
35 at 59.
36 Quigley, op cit, at 1061.

In Switzerland, both foreign awards and international awards may be enforced under the *Loi federale sur le droit international privé* - with different defences applying in each case. It would seem that a foreign award is one made outside of Switzerland, but the Convention may still be relevant with regard to international arbitration - Article 192(2) of the *Loi.*

In the United Kingdom, the 1996 Act (as did the 1975 Act) defines "Convention award" as one which is made in the territory of a state other than the United Kingdom. Similarly, in Australia, the *International Arbitration Act* 1974 provides for the enforcement of "foreign awards", which are defined as awards "made . . . in a country other than Australia". The issue then arises as to what is meant by "made."

What does "made" mean in relation to a arbitral award?

Arbitrators must state, on the face of the award, the place of the award. The place where an award is "made" is said to be "the place of the arbitration" in the legal sense. [37] This is also referred to as the "seat" of the arbitration. [38] The legal place of an arbitration, or the arbitral seat, must be distinguished from the physical place of the arbitration. The arbitral seat:-

> " . . . is by no means necessarily identical with the place or places where hearings are being held . . ." [39]

Van den Berg gives as an example an arbitration where the hearings might take place in Cairo and New York and the arbitrators sign the award in their respective domiciles, wherever those may be. The award, however, could be stated to have been "made" in Stockholm.

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37 van den Berg, "When is an Arbitral Award Nondomestic under the New York Convention of 1958?" *Pace Law Review*, Volume 6, Number 1, (1985), at 6.

38 ibid.

Mann also notes that the place where an award is "made" (the arbitral "seat") is not necessarily the place where hearings are held, or where the arbitrators reside. [40] Mann continues that this place (or seat) is the place fixed as such in the parties' contract, or submission, or "is found to be the central point of the arbitral proceedings." [41]

These views were not shared by the House of Lords in *Hiscox v Outhwaite* [42]. The parties had submitted to arbitration in London, under English law and the arbitrator had signed the award and noted it as having been made, in Paris. Lord Oliver, who delivered the speech of the House, referred to Mann's comments from the article noted above in Arbitration International. His Lordship said that whilst the reasoning of Dr Mann would "make very good sense" if the inquiry were as to where the award "ought to be deemed to be made" from the point of view of legal convenience and the parties' intentions, it did not accord with the construction of the *Arbitration Act* 1975. (The *Arbitration Act* defined a "Convention award" as one "made in the territory of a State, other than the United Kingdom"). Lord Oliver said that an award was "simply a written instrument" and that:-

> "A document is made when and where it is perfected. An award is perfected when it is signed . . .
>
> Whilst therefore, I find it anomalous and regrettable that the fortuitous circumstance of a signature in Paris should stamp what was clearly intended to be an award subject to all procedural regulations of an English arbitration with the character of a Convention award, I find the conclusion that it did irresistible . . ." [43]

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39 ibid.
40 Mann, "Where is an Award 'made'?" 1 *Arbitration International*, 1985, 107, at 108.
41 ibid.
42 [1992] 1 AC 562.
43 op cit, at 594-595.

It is not clear from either the Court of Appeal [44] or House of Lords report what the circumstances were of the arbitrator executing the award in Paris. In the Court of Appeal, Donaldson MR referred to this fact as "(o)ne of the mysteries of the case". In the House of Lords, Lord Oliver seemed to presume that the arbitrator had simply changed residence from England to Paris prior to executing the award, so it may be that the circumstances of the execution were indeed fortuitous.

As it stood, the case was authority for the proposition that what would otherwise be a domestic award could be brought under the Convention merely by having the arbitrator execute the award in another jurisdiction.

For Mann and van den Berg, the establishing of the legal place of arbitration is related to choice of law issues:-

> ". . . there is no need to agree to arbitrate in one country under the arbitration law of another country. The proper position is that . . . *the parties have the freedom to designate the applicable arbitration law by designating the place of arbitration* . . . the arbitration law of the country where the arbitration takes place governs the arbitration. The place of arbitration in this sense is determined by the parties in their arbitration agreement." [45] (original emphasis).

In other words, the parties, by choosing the legal place of the arbitration, thereby choose the applicable arbitration law (*lex arbitri*). Must, however, an arbitration be "anchored" to a particular judicial system in this way? Can a system of law, which is not a municipal legal system, be applied as the procedural law of an arbitration? Can a legal system which is not that of a State be applied as the substantive law? What is

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44 [1991] 2 WLR 1321.

45 van den Berg, op cit, at 45. The author also notes (ibid) that the parties can, of course, leave the fixing of the place of arbitration to a third party, such as the organisation under whose rules the arbitration is proceeding, or the arbitrators themselves.

the result if either of these scenarios should occur? These issues will be discussed in Chapter XI of the thesis.

"Commercial"

Several jurisdictions have adopted the second reservation, limiting the application of the Convention to matters which are considered "commercial" within the jurisdiction's understanding of the expression.

Traditionally, in most jurisdictions, the expression has been given a wide meaning. In the words of Campbell LC in *McKay v Rutherford*:-

> "Wherever capital is to be laid out on any work and a risk run of profit or loss, it is a commercial venture." [46]

Arbitration agreement must be valid

A prerequisite to the commencement of any arbitration proceedings must be a valid and enforceable arbitration agreement. Article II.1 provides that Courts shall recognise arbitration agreements and Article II.3 provides that Courts shall enforce agreements, with limited exceptions - where the court "finds that the said agreement is null and void, inoperative or incapable of being performed."

The validity of an arbitration clause within an agreement is not necessarily tied to the validity of the agreement. An arbitration clause, if properly drafted, is capable of being severed, under the separability principle. This enables the arbitrator to decide that the parties contract is void *ab initio*, without denying the arbitrator jurisdiction to hear the matter. In *Harbour Assurance Co Limited v Kansa General International*

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[46] 6 Moore PC 425; 13 Jur 23.

Insurance Co Limited [47], Steyn J (as he then was) said that there were a number of compelling reasons for adopting the separability principle with respect to arbitration clauses. These included party autonomy - the parties' desire to refer disputes to arbitration should be respected. Further, if the principle were not applied, a party could avoid arbitration by asserting the whole agreement (including the arbitration clause) was void; and it preserved the "perceived effectiveness" of arbitration as a neutral method of dispute resolution. This was vital to the machinery of commerce and therefore:-

> ". . . full recognition of the separability principle tends to facilitate international trade." [48]

In *Prima Paint v Flood & Conklin* [49], the Supreme Court of the United States confirmed that arbitration clauses are separable and will encompass arbitration of a claim that the principal contract was induced by fraud. If the arbitration agreement itself was procured by fraud, however, the jurisdiction to hear any complaint must remain with the court.

In New South Wales, the concept of separability was initially rejected [50] by the Court of Appeal, but then accepted. In *Ferris v Plaister*, Kirby P said:-

> "The primary judge was right to . . . solve the apparent illogicality of permitting the arbitrator to uphold an attack on the validity of the contract ab initio (*sic*) on the footing that an arbitration clause constitutes a severable

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47 [1992] 1 Lloyd's Rep 81.

48 op cit, at 93. The decision of Steyn J was reversed on appeal (*Harbour Assurance Co (UK) Ltd v Kansa General International insurance Co Ltd* [1993] QB 701), but only as to the effect of previous authority. The Court of Appeal otherwise endorsed Steyn J's comments - see, eg, Ralph Gibson J at 709.

49 388 US 395 (1967).

50 In *IBM Australia Limited v National Distribution Services Limited* (1991) 22 NSWLR 466.

agreement between the parties. It does not fall with the avoidance of the contract in which it is contained." [51]

It may also be the case that an arbitration agreement will be recognised as valid for the purposes of the New York Convention, even though it may offend the law of the agreed *situs*. In *Rhône Mediterranée Compagnia Francese di Assicurazioni e Riassicurazoni v Achille Lauro* [52] the parties had chosen Naples as the place where arbitration was to take place. The agreement called for the appointment of two arbitrators. Under Italian law, however, an agreement which envisages the appointment of an even number of arbitrators is void.

The appellants argued that the law of the place of arbitration was determinative for the purposes of Article II.3. The Court of Appeals (Third Circuit) noted the contrast between Articles II and V. With the latter, its various sections have governing law provisions – usually, that chosen by the parties, or in the absence of such choice, that of the place where the arbitration is to take place. Article II.3, on the other hand, provides no guidance as to what law is to be applied in making any determination. The Court noted that commentators had suggested various solutions – ranging from the law and policies of the forum state, to conflicts rules, or the law of the place where the arbitration agreement was executed.

It was held that the law "implicitly referenced" by Article II was the law of the United States; 9 USC §203 provides that actions under the Convention are deemed to arise under the laws and treaties of the United States. As the laws of the United States favoured the enforcement of arbitration clauses, the parties would be ordered to arbitrate. The agreement could only be regarded as null and void when it was subject to:-

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51 op cit, at 484.
52 712 F.2d 50 (Third Circuit, 1983).

> " . . . an internationally recognised defence such as duress, mistake, fraud, or waiver." [53]

The requirements of Italian law might well mean that an award could not be enforced in Italy; it might, however, be enforced elsewhere. A breach of the procedure which regulated the number of arbitrators would not be fatal to enforcement. Another forum would be entitled to ignore the procedural defect and permit enforcement. Article V provides that enforcement " . . . *may* be refused on the basis of the law of the country where it was made." [54] In other words, an adverse finding under Article V would not automatically result in refusal to enforce – a discretion existed to permit enforcement.

Are the defences contained in the Convention exclusive?

In the main, decisions of United States courts have confirmed that the defences contained in the New York Convention to requests for recognition and enforcement are exclusive. In *Parsons & Whittemore Overseas Co Inc v Societe Generale de L'Industrie du Papier* (RAKTA) [55], the Court stated that:-

> " . . . the provisions of Article V and the statute enacted to implement the United States' accession to the Convention are strong authority for treating as exclusive the bases set forth in the Convention for vacating an award." [56]

Shortly afterwards, this approach was also adopted in *Ipitrade International SA v Federal Republic of Nigeria* [57], where Gasch J of the United States District Court (DC) said that Article V of the Convention:-

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53 op cit, at 53.
54 op cit, at 54.
55 508 F. 2d 969 (Second Circuit 1974).
56 op cit, at 977.
57 465 F Supp. 824 (District of Columbia, 1978).

" . . . specifies the only grounds on which recognition and experiment of a foreign arbitration award may be refused." [58]

In *Brandeis Instel Limited v Calabrian Chemicals Corp* [59], the respondent ("Calabrian") argued that the defence of "manifest disregard of the law" [60] was indirectly available in an action for enforcement of a Convention award. Calabrian agreed that if the arbitrator had shown "a manifest disregard of the law", then to enforce an award in those circumstances, would violate public policy, thereby offending against V.2(b) of the Convention. The Court rejected Calabrian's argument, stating that a public policy defence would only succeed where basic notions of morality and justice were offended. [61]

Consequently, "manifest disregard" was not available as a defence. This was founded on public policy - applying the words of the Supreme Court in *Scherk v Alberto Culver* [62], to the effect that the goal of the Convention was the encouragement of the recognition and enforcement of foreign awards and the imposition of standards by which awards are observed and enforced. [63] This could be better achieved by applying only a narrow concept of "public policy" - to allow American judges to embark on an investigation as to whether foreign arbitrators had disregarded foreign law, would be "a clear derogation of the public policy underlying the Convention." [64]

In *Dworkin-Cosell Interair Courier Services Inc and ors v Avraham* [65], an arbitration had taken place following the dismissal of the respondent from the employ of the

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58 at 826.

59 656 F Supp. 160 (SDNY, 1987).

60 "Manifest disregard of the law" is not defined in the Act. The phrase originated in *Wilko v Swan* 346 US 327 (1953) and is a defence available in domestic arbitration in the United States. The concept involves "something beyond and different from a mere error in the law or failure on the part of arbitrators to understand or apply the law" – *Siegel v Titan Indus Corp* 779 F.2d 891 (Second Circuit, 1985), at 892. Generally, for the defence to be made out, arbitrators must have understood and correctly stated the law, then proceeded to ignore it - *Merill Lynch, Pierce, Fenner and Smith, Inc v Bobker* 808 F.2d 930 (Second Circuit 1986), at 937.

61 op cit, at 166.

62 417 US 506 (1974).

63 op cit, at 167.

64 ibid.

65 728 F Supp 156 (SDNY, 1989).

plaintiff ("Dworkin-Cosell"). The respondent was both a director and shareholder of Dworkin Cosell. Article 2 of the arbitral award had provided (*inter alia*) that the respondent was entitled to nominate a director of Dworkin-Cosell for a period of six months and that the parties were to negotiate in good faith for the sale of shares in Dworkin-Cosell held by any party. The arbitrator expressed the award to be, except for Article 2, in full settlement of all claims and counter-claims submitted to arbitration. After the publication of the award, the respondent then sought the payment of further moneys from Dworkin-Cosell, threatening legal action, if it was not paid. Dworkin-Cosell's response was the commencement of a court action, for orders that the award barred further claims. In those proceedings, the respondent sought confirmation of the award.

In court, Dworkin-Cosell alleged that the award was "not final" and was also "ambiguous." They also argued that, should the judge confirm the award, it should only be on the basis that the respondent was barred from commencing litigation over the moneys he claimed were owed to him.

Stanton J commenced by noting that the "general rule" was that the defences set out in Article V of the Convention were exhaustive. His Honour noted further that the authorities [66] to which he referred, however:-

> " . . . did not examine a challenge to the award's finality or lack of ambiguity." [67]

Stanton J then referred to *Ipitrade International SA v Federal Republic of Nigeria* [68] and *Fertilizer Corporation of India v IDI Management* [69], which, His Honour stated, were both authority for the proposition that "finality" was required with awards. Stanton J accepted Dworkin-Cosell's arguments and remitted the award to the arbitrators.

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66 *Parsons & Whittemore v Societe General de L'Industrie du Papier*, op cit and *Brandeis Instel V Calabrian Chemicals*, op cit.

67 op cit, at 161.

68 op cit.

It is submitted that these two cases do not, however, go as far as Stanton J suggests. In *Ipitrade*, which centred on a claim for sovereign immunity, Gasch J noted that an award rendered under Swiss law, was, under that law, "final and binding". (Gasch J also stated that the defences under Article V were exhaustive). [70]

In *Fertilizer Corporation of India*, the Court considered Article V.I(e) and reviewed the law of India, to ascertain, if awards were considered "binding" even if subject to appeal. The Court than stated that it considered that the award in question was "final and binding" for the purposes of the Convention.

With respect to Stanton J, it is submitted that use of the word "final" was extraneous to both the decisions His Honour referred to. The requirement under the Convention is that awards must be "binding". In both these cases, the Courts were referring to national legal systems and the status of awards under those systems.

Again, with respect, it is difficult to see why it was necessary or permissible to go outside the words of the Convention. One must look to the words of the Convention. There is no reference to the fact that an award be "final". Whilst the award in *Dworkin-Cosell v Avraham* did state that all matters were settled, with the exception of those in Article 2, there are a number of other possibilities that the Court might have entertained. If the parties were left to negotiate over the sale of shares, then this part of the award might have been regarded as severable; a further award might have been made in this respect.

Further, if, as Dworkin-Cosell argued, the award precluded the recovery of further moneys by Avraham, then the trial judge should have made a ruling as to what matters the award covered. This would have either ended the disputes or left Avraham free to pursue further claims, subject of course, to any estoppel defences.

The "exclusivity" of Article V was reaffirmed in some recent decisions. In *Yusuf Ahmed Alghanim & Sons WLL v Toys "R" Us Inc.* [71], the Court noted that:-

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69 517 F. Supp 948 (SD Ohio, 1981).
70 *Ipitrade*, op cit, at 826.
71 126 F.3d 15 (Second Circuit, 1997).

> "There is now considerable case law holding that, in an action to confirm an award rendered in, or under the law of, a foreign jurisdiction, the grounds for relief enumerated in Article V of the Convention *are the only grounds available* for setting aside an arbitral award." [72] (emphasis added).

The Court stated that permitting parties to avail themselves only of those matters referred to in the Convention was:-

> " . . . consistent with the Convention's pro-enforcement bias." [73]

In *Industrial Risk Insurers v MAN Gutehoffnungshütte GmbH* [74], the Court also confirmed that the defence that the award was "arbitrary and capricious" was not available, nor was any defence not specified in the Convention; and in *Sarhank Group v Oracle Corporation* [75], the United States District Court (Southern District, New York) confirmed that the Convention's defences provided the "sole basis" for resisting the enforcement of awards. [76]

One Australian decision, however, takes the opposite approach. In *Resort Condominiums International Inc v Bolwell and anor* [77], Lee J of the Supreme Court of Queensland relied on *Dworkin-Cosell* in stating that defences to an action for enforcement were not confined to the specific matters set out in the Convention. [78]

As noted above, *Dworkin-Cosell* is not representative of the United States authorities. The decision has been criticised on this aspect. [79]

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72 op cit, at 20.
73 ibid.
74 141 F.3d, 1434 (Eleventh Circuit, 1998).
75 2002 US Dist LEXIS 19229 (SDNY).
76 op cit, at 12.
77 118 ALR 655 (1993).
78 at 675. His Honour also accepted that, quite apart from the issue of whether the Convention's defences were exclusive, there was a "general discretion" available not to enforce awards - ibid. This was based on the omission of the word "only" from the opening words of s8(5) of the Australian *International Arbitration Act* 1974.
79 Buckingham and Werner, "The Internationalisation of Public Policy: The Road to Avoidance

Jurisdictional link

In order for a court to enforce an award, there must be some link between the jurisdiction in which the award is sought to be registered and the defendant. In *Transatlantic Bulk Shipping Ltd v Saudi Chartering SA* [80], the petitioner sought to confirm an award, made in London, in New York.

The defendant resisted, claiming that the New York courts had no jurisdiction over the respondent, which was a Panamanian corporation whose principal place of business was in Greece. It had no presence in New York and did not conduct business there. The underlying contract had not been made in New York.

The petitioner argued that jurisdiction was attracted because of the New York Convention and that the United States had implemented the Convention in its federal legislation.

Whilst Article 9 USC §201 provides that actions or proceedings under the Convention are deemed to arise "under the laws and treaties of the United States" and gives jurisdiction to the District Courts of the United States to hear such "actions or proceedings", the Court said that this:-

> " . . . did not give the courts power over all persons throughout the world who have entered into an arbitration agreement covered by the Convention. Some basis must be shown, whether arising from the respondent's residence, his conduct, his consent, the location of his property or otherwise, to justify his being subject to the court's power." [81]

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or the Application of International Commercial Arbitration?", *Australian Construction Law Newsletter*, Issue 75, December 2000, 27, at 31.

80 622 F. Supp 25 (1985) (SDNY).

81 op cit, at 5.

This was followed in *Glencore Grain Rotterdam BV v Shivnath Rai Harnarain Co* [82]. It would seems that most courts would require a jurisdictional link (to the place of enforcement) of some kind before allowing an award to be recognised and enforced.

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[82] 284 F. 3d 1114 (Ninth Circuit, 2002).

PART II

PUBLIC POLICY GENERALLY

PUBLIC POLICY FAVOURS ARBITRATION

PUBLIC POLICY AND THE ENFORCEMENT OF AWARDS

CHAPTER IV

PUBLIC POLICY

"*Intervention by the judges on the basis of public policy has a long history.*" [1]

Public policy and arbitration

It will be argued that public policy occupies an essential place in arbitration. In order to more fully explain why that is so, it is proposed to examine public policy on a wider level - its place in legal systems generally.

Public policy historically - common law

Judges in common law courts have applied public policy (not necessarily always called by that name) for centuries.

The historical application of public policy had two distinct phases - firstly, when the common law system was in its infancy, there was little by way of legislation or precedent. In these circumstances, public policy, although it was not called such, was applied in a "half-conscious" way and:-

> " . . . probably pervaded the whole legal system when law had to be made in some way or other . . ." [2]

The application of public policy then became "conscious" when it was actively used to resolve specific legal problems. [3]

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1 Bell, *Policy Arguments in Judicial Decisions*, Clarendon Press, 1983, at 156.

2 Winfield, "Public Policy in the English Common Law" (1928) 42 *Harvard Law Review*, 76, at 77.

3 Winfield, op cit, 77.

Winfield suggests that there was in fact a paradox - when public policy "pervades" the law, "nobody is aware of its existence." [4] During public policy's first "phase", nonetheless:-

> " . . . it is possible to discover already in the earlier history the essential characteristics of the doctrine. There is no question of statute or written law. The doctrine, concealed under widest generalization, operates, in fact, because of some gap in the law, though only where the dominant general consideration is the good of the community - the supreme law - with, it may be, some special consideration for the rights or interests of individuals other than those immediately concerned in the matter the subject of the suit." [5]

It is suggested that it is easy to see the significance of a body of general principle when the law is in its infancy. The body of principle guides the application of the law and underlies the ways in which the law develops. As precedents and statutes are created and grow, general principle is not applied directly quite as much as it once was. Nonetheless, its moral authority is undiminished and it remains the inspiration for judicial decision-making in areas where there is perhaps a gap in the law, or where there is an agreement or an activity which threatens the public good.

As noted, the phrase "public policy" itself did not appear for some time. Knight states that it was probably first used by Lord Mansfield, in *Holman v Johnson* [6], where His Lordship stated:-

> "The principle of public policy is this: Ex dolo malo non oritur actio. No court will lend its aid to a man who founds his cause of action on an immoral or illegal act." [7]

Despite this (probably) being the first instance of the use of the expression, its actual scope was too narrowly put by His Lordship. [8] Other judicial pronouncements took

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4 Winfield, ibid.
5 Knight, "Public Policy in English law", (1922) 38 *Law Quarterly Review*, 207, at 208.
6 (1775) 1 Cowp. p.341.
7 Knight, op cit, at 209.

the principle of public policy beyond "bare immorality and illegality", applying it where contracts were injurious to the interests of the public or against public benefit. [9]

Public policy - related to natural law?

Walker states that the starting points for natural law (which has endured through a number of phases and adaptations) have always been " 'reason' and the 'nature of man' ". [10] It seems, however, that in the common law of England, "reason" leant more toward the practical than the abstract. Paton states that whilst some elements of natural law theories permeated English law and that English law was as open as any legal system to ethical influences, the application of public policy tended to be on a practical, rather than philosophical, basis. This was because attention was turned towards striking down individual contracts, rather than setting philosophical contexts for legal relationships. [11]

In *Commentary upon Littleton*, Coke said that reason was "the life of the law", such reason arising out of "study, observation and experience", rather than being man's "natural reason". [12] Coke's reference to "natural reason" (distinguishing this from "practical reason") seems to be a reference to natural law theories.

Certainly, from this passage, Coke would deny that the law was based on "natural" reason, but was based instead on reason derived from practical experience.

It may be, however, that, especially in earlier times when statute and precedent were largely lacking (and the law had to be "made in some way or other"), inspiration for the establishment of legal principles was inspired by concepts derived from the notion of a superior law.

As the power of Parliament grew and eventually became supreme, however, references to aspects of a "superior" law decreased. These were replaced by

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8 Knight, op cit, at 210.
9 ibid.
10 Walker, *Oxford Companion to Law*, Clarendon Press, 1980, at 868.
11 Paton, *Jurisprudence*, Clarendon Press, Second Edition, 1951, at 97-98.
12 Winfield, op cit, at 82.

references to the rule of reason and natural justice. [13] Further, jurists in the Middle Ages had started to place natural law within concepts of divine law. As England severed its ties with the Church of Rome, the idea of a natural law based on or within divine law became less appealing. Public policy began to "split" from natural law thinking. [14]

Much of the reasoning of English judges and lawyers in this context, nevertheless, remained true to natural law concepts, even though there may have been no direct references to "natural law" as such. [15]

The expression "inconvenience" was also used. [16] Coke noted "and emphasised" the maxim *nihil quod est inconveniens est licitum* [17]. Coke's view of what was impermissible was not always consistent, however. Sometimes a narrow view was taken - public policy was not concerned with *mala in se* [18], but with *mala quid prohibita* [19], which were "repugnant to the state" or against rules or maxims of law. [20]

The consequence of this inconsistency, Winfield states, is that it is difficult to draw any definitive meaning from Coke's work on the question of public policy. The significance of Coke's dicta (which otherwise "would not be worth citing") says Winfield, lies in the use made of them by His Lordship's successors. [21]

Shortly after the death of Coke, Sheppard's *Touchstone of Common Assurances* was published. [22] Sheppard utilised a phrase which, like Coke's, was to come to prominence in the law reports. Sheppard referred to such conditions in deeds or limitations which are "against public good" as being void.

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13 Haines, *The Revival of Natural Law Concepts*, Harvard University Press, 1930 (obtained at URL www.constitution.org - p. 24 of that version).

14 Winfield, op cit, at 87.

15 Haines, op cit, at 25-26.

16 In the *Duke of Norfolk's* case (1681) 3 Ch. Cas. 1, Lord Nottingham, in confirming the validity of a disposition which provided for the carrying over of an estate upon a contingency to happen in a lifetime, was asked where His Lordship would place a limit, so as to prevent perpetuities. His Lordship responded - "I will stop wherever I find a visible inconvenience." (Reproduced in Winfield, op cit, at 85).

17 "Nothing inconvenient is lawful"; Winfield, ibid.

18 "Wrongs in themselves."

19 "Wrongs which are prohibited by human laws."

20 Winfield, op cit, at 82.

21 Winfield, op cit, at 83.

22 In 1641.

Egerton v Brownlow - a "high water" mark

In 1853, there occurred the landmark decision of *Egerton v Brownlow*. [23] The Earl of Bridgewater had made a number of provisions in his will, one of which was the disposition of vast areas of his estates to Lord Alford, on the condition that Lord Alford acquire the title of Duke or Marquis of Bridgewater. If neither title was obtained, then the devise would be void, and pass over to another branch of the Earl's family, subject also to the obtaining of a title. Lord Alford died without acquiring either title and his heirs brought action against the trustees, claiming that the condition imposed was void.

The case reached the House of Lords. Their Lordships requested the opinions of the judges on the issues involved.

The first issue was whether the testator's condition was a condition precedent or a condition subsequent – if it were the former, no estate could vest in the appellant - but if it were the latter, the second issue was whether the condition was then void on the grounds of public policy?

The majority of the judges advised the House of Lords that the condition was a condition precedent, and that the devise imposing the conditions was valid.

Pollock CB was in the minority. His Lordship's views are an important statement on the nature of public policy. His Lordship reviewed a number of authorities, as well as the writings of Sheppard and Coke and said:-

> "I think, therefore, I am bound to lay down this principle as a clear and undoubted maxim of law, that if this condition be 'against the public good' (the expression in Sheppard's Touchstone), if it be 'repugnant to the State' (the expression in Coke), it is void." [24]

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23 10 ER 359.

24 op cit, at 415.

Pollock CB found firstly that the condition was a condition subsequent. His Lordship then turned to the question of its validity. His Lordship noted that there was no direct authority on the point as to whether it was:-

> " . . . competent to the owner of an estate to create, by deed or will, one or more contingent remainders, or conditional limitations, which shall depend upon the exercise of the royal prerogative in creating a peerage in a particular family, with a particular title, and with prescribed limitations." [25]

Pollock CB stated that these issues raised questions of public policy. Public policy was recognised as a "ground of decision" in relation to covenants, contracts and "other matters." [26] His Lordship continued:-

> "This doctrine of the public good or the public safety, or what is sometimes called 'public policy', *being the foundation of the law*, is supported by decisions in every branch of the law; and an unlimited number of cases may be cited as directly and distinctly deciding upon contracts and covenants as the avowed broad ground of the public good and on that alone . . . ". [27] (emphasis added).

His Lordship then said:-

> "I think no man can leave his property clogged and conditioned by his own personal views of public affairs, or by his posthumous ambition . . . he cannot make his political opinions run (like a covenant) with his land; he may leave it to whom he pleases, but it must be unfettered by any condition bearing upon the public welfare . . ." [28]

The testator's condition was void, His Lordship said, as it would end to corrupt, not only the ranks of the peerage, but the Crown itself. The testator had seemingly

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25 ibid.
26 op cit at 416.
27 op cit, at 417.
28 op cit, at 419.

regarded a peerage as a "bauble", ignoring the fact that a peer has public duties of the highest order and which are of great importance to the public welfare. [29]

The testator had created a "dangerous pecuniary interest" for the devisee to attempt to obtain the peerage.

The creation of peers was entirely the prerogative of the Crown and such prerogative must be exercised:-

> " . . . for the good of the country . . . and solely with reference to the public welfare." [30]

It was accordingly against public policy to bequeath property subject to capricious conditions, dependent upon a public act. [31]

Pollock CB not only emphasised the importance of public policy in safeguarding the public good, His Lordship also emphasised that there was a clear duty to apply public policy:-

> "My Lords . . . am I not justified in saying that, were I to discard the public welfare from my consideration, I should abdicate the functions of my office – I should shrink from the discharge of my duty?" [32]

Further, His Lordship continued, this duty has to be observed, no matter that judges do not have an exclusive hold on what might constitute the public interest:-

> "My Lords, it may be that Judges are no better able to discern what is for the public good than other experienced and enlightened members of the community; but that is no reason for their refusing to entertain the question, and declining to decide upon it." [33]

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29 op cit, at 420.
30 ibid.
31 op cit, at 421.
32 op cit, at 419.
33 ibid. His Lordship's comments might be interpreted as justifying recourse to extra-judicial sources, in order to determine public interest.

The fact that this duty exists was confirmed by Roche J in *James v British General Insurance Company Ltd* [34], where His Honour stated:-

> "In cases such as this, in which considerations of public policy arise, the rights and duties of judges are clear. They have to attend to matters of public policy. Any dispute about that, and there was apparently some dispute about it as late as 1853, was set at rest by the well known case of *Egerton v Earl Brownlow*, where it was established that it is the duty and the right of Courts to refuse to enforce contracts or dispositions of property which are offensive and obnoxious to public policy." [35]

The House of Lords also disagreed with the opinions of the majority of the judges. Lord Lyndhurst, as had Pollock CB, saw the devise as interfering with the prerogative of the Crown. His Lordship stated that whilst, in reality, many peerages were created for political reasons, any person seeking a peerage because of the circumstances created by the testator, would have a tendency to support without question those (ie, advisers and ministers of the Crown) who could bring about the desired result. This would undoubtedly corrupt the approach to the public duties imposed on a peer. [36]

Lord Brougham also thought that such a situation could lead to the undue influencing of "the dispensers of royal favour"; so did Lord Truro. [37] Lord St Leonards saw the devise as an embarrassment and an insult to the Crown, in attempting to point out that a person should have a particular title and to make further provision if that could not be achieved. [38]

Winfield concludes that the opinion of Pollock CB:-

> " . . . represents what English law always has been and still is." [39]

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34 [1927] 2 KB 311.
35 op cit, at 321.
36 op cit, at 424.
37 op cit at 428 and 439.
38 op cit, at 452.
39 Winfield, op cit, at 90.

Interaction of social interests and law

Pollock CB saw that the protection of the public interest is at the heart of public policy. Knight says that the essence of public policy is that it is applied for "the good of the community." The author equates this to the "supreme law", lying at "the foundation of the whole system of English law, of the State itself."

As public policy is the benchmark for judicial legislation, it is undisputed that public policy is part of the law itself. It does *not* operate outside the law, like some "paramount censor" of law and rights. [40] Consequently, public policy:-

> " . . . can . . . never involve a clash between 'policy' and 'law' . . . Insofar as the 'public policy' rule for the particular situation can be regarded as settled then the conflict is between two rules of law one of which is overriding . . . Insofar as it is not settled, as the case is 'new and unprecedented', the conflict is of *de facto* interests which call for legislative adjustment by the court." [41] (original emphasis).

The context for the operation of public policy is the interests of society as a whole. Social interests exist independently of law – but they:-

> " . . . are the important part of the context in which law must operate, and the whole of the subject matter upon which it must operate . . . But no one interest . . . (*is*) . . . inherently better than others . . . all must be taken in to account in assessing the relation of law to society." [42]

The adjustment of rights is at the heart of public policy. Stone goes on to say that judges "may not prohibit 'everything' they think evil", and "may not act *at large in each case*" (original emphasis). Stone asks whether applying public policy is a

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40 Stone, *The Province and Function of Law*, Maitland Publications, Second Printing, 1950, at 494.

41 op cit, at 499.

42 Stone, op cit, at 489.

mechanical process – or does it involve an element of "creative choice?" [43] The latter view is preferred. In applying settled public policy rules:-

> " . . . those rules within their ambit are rules of the common law like any other rules. Since they are common law rules, however, they are subject to the same process of erosion, transformation and supplementation which . . . characterises much judicial activity." [44]

Given that public policy is part of the law, firstly, such creativity becomes necessary as the law evolves; secondly, the processes of such creativity must be quite similar to that which is found in judicial decision-making generally:-

> "In this field, just as new principles of torts may develop, so presumably may new principles of public policy." [45]

It is suggested that this is correct. Public policy must be flexible, in order to accommodate societal change.

It must also follow that as public policy precedents can be set, courts are bound by rules of interpretation and application to the same extent that they are bound by other legal rules. [46] It is in this context that Stone, as did Pollock CB in advising the House of Lords in *Egerton v Brownlow* [47], emphasises that the application of public policy by the courts is not so much a question of the court's power to do so, but of its *duty* to do so. [48]

Not to apply public policy where necessity dictates that it must be applied, is, consequently, a breach of duty.

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43 Stone, op cit, at 497.
44 ibid.
45 ibid.
46 Stone, op cit, at 500.
47 op cit.
48 Stone, ibid.

A definition of public policy

Before looking at some more recent pronouncements on public policy, some further observations by Winfield and Knight (as well as Stone) are worth considering.

Winfield notes that public policy can sometimes be elusive, [49] but nonetheless asks – "what does public policy mean?" and attempts a definition:-

> " . . . a principle of judicial legislation or interpretation founded on the current needs of the community." [50]

Hence, public policy is a legal principle and it is founded on concepts of the public good. It is invoked by courts to justify intervention in matters where an agreement (or part of an agreement) is considered injurious to the public welfare.

The use of the word "current" in Winfield's definition indicates that public policy must also be flexible and adapt to changing community interests. Winfield continues by saying that the definition means that the interests of the whole of the public must be taken into account, even though, in reality, many decisions based on public policy may only affect one section of the community. This should not prevent judges, however, weighing the interests of the whole of the community in applying public policy considerations. If a decision favours a particular group, then all that should mean is that their interests are (at least in relation to the matter at hand) compatible with those of the community as a whole.

Further, any difficulty in discerning public interest or identifying public policy should not lead to the absolving of the requirement to ascertain what it is:-

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[49] Winfield, op cit at 91 and 92. The author notes the famous metaphor of Burrough J in *Richardson v Mellish* (1842) 2 Bing 229, regarding public policy as being an "unruly horse". In the same vein, Knight notes a period in the 19th Century of "scepticism and hesitation" with regard to applying public policy, in that some judges became concerned as to the place of public policy within the law. This passed, however, and the courts began to reapply the broad principles invoked in earlier cases (Knight, op cit, at 212 - 215.)

[50] ibid.

> " . . . judges are bound to take notice of it and of the changes which it undergoes." [51]

Winfield and Knight take what might appear to be different stances, at least in degree - for Winfield, public policy is no longer the "whole spirit" of English law, but remains "part" of its spirit. [52] Knight states that public policy is no less than:-

> ". . . the one principal rule at the foundation of the whole system of English law, of the State itself . . . the essential element in the idea of the King's justice, it is, in actual fact as well as in principle, the ever-obliging authority and available instrument for what may be nothing other than positive judicial legislation, independent, absolutely, in the absence of statute." [53]

These views are not necessarily inconsistent. To say that public policy is no longer the "whole spirit" of the law might be seen as only acknowledging that the range of cases where public policy (as overtly stated to be such) might be applied has diminished, not because public policy has become less important, but that the legal system has evolved towards much greater specificity than previously existed, via increasing legislation and use of precedent.

What was initially public policy has undoubtedly passed into legislation and inspired "judge-made" law.

Both Winfield and Knight certainly reinforce the fact that public policy reflects the overall public good - and that there is a duty on courts to ascertain and apply it.

"Free rein" for public policy

Further still, whilst there are factors which keep public policy in check [54], any "fencing" of public policy will "not be of the slightest use in developing the law." [55]

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51 Winfield, op cit, at 92-93.

52 ibid.

53 Knight, op cit, at 219.

54 Eg, it must not conflict with legislation, or clear rules of the common law. The second of these is debatable. Common law rules may change over time - and the changing of public policy considerations can lie behind changes to the common law.

It is suggested that this is a most significant comment. If public policy is read down, then that can only lead to imbalance in the adjustment of social interests and the atrophying of the law itself.

There might be a question as to how can public policy be read down, if it is so elusive? How can it be read down if we do not know what it is?

There is a difference between struggling to determine public policy, and refusing to acknowledge the duty to apply it. The former presents a difficulty (but one which does not alleviate the court's duty - see the above quote from Pollock CB [56]), the latter is impermissible.

Matters requiring intervention on the basis of public policy

At this stage, it is perhaps appropriate to consider some instances in which courts have intervened on the basis of public policy.

A summary compiled in 1947 [57] refers to matters such as breach of international comity; "irregular sexual connections"; unreasonable restraint of trade or of liberty; evasion of legal obligations; the purchase or sale of honours or public offices; defeating or delaying creditors and perversion of the course of justice, as having "objects immoral" or being contrary to public policy. [58]

In 1950, Stone identified matters such as the interests of the State in times of conflict; violations of the law of friendly States; the social interests in the integrity of political institutions (which can be challenged by contract to influence government policy for private purposes); the "great social interest" in the integrity of legal and judicial institutions; the social interest in the maintenance of morals, including sexual matters and "dishonest dealings generally"; and the policy against restraint of trade. [59]

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55 Winfield, op cit, at 98.
56 n.33.
57 In Winfield et ors, *Jenks' English Civil Law,* Fourth Edition, Butterworths, 1947.
58 Winfield, in *Jenks*, op cit, at 76-77.
59 Stone, op cit, at 501-502.

Most of these matters clearly are of permanent importance - the integrity of legal and judicial institutions; perversion of the course of justice; the maintenance of morals and prohibiting dishonest dealings are obvious examples. Others may not be in this category - there may not be such interest nowadays as to whether a lease on an apartment is taken "for the purpose of enabling [*the defendant*] to receive the visits of the man whose mistress she was." [60]

It is clear that, as society changes, the focus of public policy will change. Public policy will continue to be relied upon to strike down immoral contracts, but what is regarded as "immoral" may change over time. Evolution, of course, is not unique to public policy considerations. In the High Court of Australia decision, *Re Wakim; ex parte McNally* [61], a case involving constitutional issues, McHugh J noted that:-

> " . . . many words and phrases of the Constitution are expressed at such a level of generality that the most sensible conclusion to be drawn from their use in a Constitution is that the makers of the Constitution intended that they should apply to whatever facts and circumstances succeeding generations thought they covered.
>
> [*His Honour gave some examples of terms used and continued:*-]
>
> The level of abstraction for some terms of the Constitution is, however, much harder to identify. . . . Thus, in 1901, "marriage" was seen as meaning a voluntary union for life between one man and one woman to the exclusion of all others. If that level of abstraction were now accepted, it would deny the Parliament of the Commonwealth the power to legislate for same sex marriages, although arguably "marriage" now means, or in the near future may mean, a voluntary union for life between two *people* to the exclusion of others." [62] (original emphasis).

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60 *Upfill v Wright* [1911] 1 KB 506, where the plaintiff landlord was prevented, on the basis of public policy, from recovering rent from the defendant because of the landlord's knowledge of the "immoral purpose" of the letting.

61 (1997) 198 CLR 511.

62 op cit, at 552, 553.

So it may be for public policy, which also is built on generalities and abstractions. The themes remain constant - eg, "immorality". As noted above, however, views of what constitutes immorality will change. The courts' task at any time is to establish what is apt for that time.

Public policy in trade and commerce

An example of public policy operating in the area of trade and commerce is the House of Lords decision in *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Limited* [63], which dealt with a covenant in restraint of trade. Lord Macnaghten noted the basis on which restraints of trade were generally considered void:-

> "The public has an interest in every person's carrying on his trade freely: so has the individual. All interferences with individual liberty of action in trading, and all restraints of trade in themselves, if there is nothing more, are contrary to public policy . . . But there are exceptions . . . It is a sufficient justification if the restraint is reasonable - reasonable, that is, in reference to the interests of the parties concerned and reasonable in reference to the interests of the public." [64]

The public interest in maintaining freedom to trade is protected by public policy. Any exception to that interest must also be referable to the public interest. His Lordship also emphasised that it is the public interest *generally* which is protected by public policy.

Contemporary statements on public policy

In more recent years, general statements about the nature and significance of public policy have remained constant with historical pronouncements. In *Lemenda Trading Co Ltd v African Middle East Petroleum Co Ltd* [65], the issue before the Court was

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63 [1894] AC 535.
64 at 565.
65 [1988] QB 448.

whether a contract for the exercising of "personal influence" should be enforced. Phillips J considered that such a contract would be against English public policy. His Honour said:-

> "The principles underlying the public policy in the present case are essentially principles of morality of general application." [66]

His Honour also said that he believed that an agreement for such a purpose, particularly where the person to be influenced was unaware of the "pecuniary motive", was "unattractive whatever the context." [67]

Another example is the judgment of Donaldson MR in *Deutsche Schachtbau-und Tiefbohrgesellschaft mbH v Ras Al Khaimah National Oil Company* [68], where, in the context of an application for the enforcement of an arbitral award, His Lordship said:-

> "It has to be shown that there is some element of illegality or the enforcement would be clearly injurious to the public good or, possibly, that enforcement would be wholly offensive to the ordinary reasonable and fully informed member of the public on whose behalf the powers of the State are being exercised." [69]

This is confirmation that public policy involves considerations of the public good. Donaldson MR also suggests a possible test - by referring to the standards of "an ordinary reasonable (and fully informed) member of the public." [70] This may have been an attempt to set up a "man on the Clapham omnibus" (or "ordinary reasonable man") test for the ascertainment of the public interest. With respect, that may be somewhat difficult - something which may have been recognised by His Lordship, by requiring that the ordinary reasonable member of the public must be "fully informed." Presumably, His Lordship meant that such a person should have a general awareness of moral issues and also be aware that there is a duty cast on those exercising the

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66 op cit, at 461.
67 ibid.
68 [1987] 3 WLR 1023.
69 op cit, at 1035.
70 ibid.

judicial powers of the State to intervene in commercial and other dealings where the public good requires it? That might be asking too much. [71] Also, who is the "community" on whose behalf the public interest is applied, in the context of an international agreement? [72]

It is submitted that His Lordship is correct, nonetheless, in stressing that it is the interests of the public which underlie the exercise of State power. Put another way, public policy exists:-

> ". . . not abstractly, for the state, but concretely, for the people . . ." [73]

Bell also touches on this. Court intervention on policy grounds can ensure:-

> " . . . the good functioning of institutions essential to the community . . ." [74]

Cheshire and North state that intervention on the basis of public policy is justified by reference to such "moral, social or economic principles" which are regarded as being "so sacrosanct" that they must be protected at all costs and without exception. [75]

Public policy in the civil law

Public policy is an important feature of civil law systems. As was noted above in this Chapter, civil law systems tend to be more norm based than the common law, incorporating in codes references to good faith and good morals, as well as to public policy (*ordre public*). Article 6 of the French *Code Civil* provides that parties may not, by private convention, derogate from laws which concern public order and good morals. [76] (It has been suggested that public order and good morals overlap, in that consideration for morality must fall within the idea of public order. The authors

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71 Questions of how courts might "find" public policy are addressed in Chapter XII.

72 Also addressed in Chapter XII.

73 Grantham, "The Arbitrability of International Intellectual Property Rights", 14 *Berkeley Journal of International Law* (1996), 173, n.62.

74 Bell, op cit, at 179.

75 Chesire and North, *Private International Law*, Butterworths, 13th Edition, at 123.

76 "*On ne peut pas déroger, par des conventions particulières, aux lois qui intéressent l'ordre public et les bonnes moeurs.*"

continue that whilst this might be so, the distinction, being "traditional", is nonetheless maintained). [77]

Public order requires that agreements which are incompatible "with the interests of society" are unenforceable. The power given to courts to annul and strike down contracts is "one of the most redoubtable prerogatives given them by the law." [78] This prerogative might be abused, if exercised by "rigid moralists, or sectarian minds." [79] The force which tempers the application of the prerogative is:-

> " . . . public opinion, the general current of ideas, that regulates the moral level of a people and creates the required kind of tolerance." [80]

The authors of Amos and Walton also refer to the interests of society as being the touchstone, noting that there is "considerable similarity" between the French and English courts in the application of public policy. [81] There is another aspect to Article 6 – *bonnes moeurs*. An agreement is offensive to *bonnes moeurs*:-

> " . . . when it offends general sentiments of duty, propriety and public decency." [82]

Ordre public and *bonnes moeurs* have been described as "twin notions" and the channels by which:-

> " . . . courts can deviate from the application of 'strict law' when prejudicial to social policies." [83]

In the area of contract law, the "twin notions" operate as "general formulations", striking down arrangements against good morals and public policy, despite the fact that no law may have been broken. [84]

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77 ibid.

78 Planiol, *Treastise on the Civil Law*, 12th Edition, 1939 (translation by Louisiana State Law Institute), at Paragraph 294.

79 ibid.

80 ibid.

81 Amos and Walton, op cit, ibid.

82 Amos and Walton, op cit, at 171.

Under the German Civil Code (*Bürgerliches Gesetzbuch* - "BGB") §138 provides that a legal transaction which offends good morals is void. [85] German Civil law is also anchored by §242 BGB, which, in the performance of agreements, requires obligors to effect performance in "good faith", with regard to common usage [86]

This provision has been developed by the courts as a "super control norm for the whole BGB." [87] The doctrine of good faith (*Treu und Glauben*) has been described as an equitable rule "governing private law in general, and contract law in particular." [88]

United States

§178(1) (contained in Chapter 8) of the *Restatement of the Law, Second, Contracts* ("Restatement"), sets out the basis on which contractual terms are unenforceable on the grounds of public policy:-

> "A promise or other term of an agreement is unenforceable on grounds of public policy if legislation provides that it is unenforceable or the interest in its enforcement is clearly outweighed in the circumstances by a public policy against the enforcement of such terms."

The Restatement notes that courts will intervene on the basis of the "need to protect some aspect of the public welfare". Examples where this can occur are in matters such as restraint of trade, impairment of family relations, a promise to commit a tort, a promise that interferes with the performance of a contract with another party, a promise by a fiduciary to breach their duty and where a party seeks restitution for performance rendered in return for a promise which is unenforceable on public policy grounds. [89]

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83 David and de Vries, *The French Legal System*, Oceana, 1958, at 134.
84 David and de Vries, op cit, at 135.
85 *"Ein Rechtsgeschäft, das gegen die guten Sitten versoßt, ist nichtig."*
86 *"Der Schuldner ist verpflichtet, die Leistung so zu bewirken, wie Treu und Glauben mit Rücksicht auf die Verkehrssitte es erfordern."*
87 Horn, Kötz and Leser, *German Private and Commercial Law: An Introduction*, Clarendon Press, 1982, at 135.
88 Beck, *Introduction to German Law* (Ebke and Finkin eds), Kluwer, 1996, at 176.
89 see §186-197.

The basis of the application of public policy in the United States seems little different to that in Europe and common law jurisdictions. Cardozo, writing extra-judicially, analyses the role and duties of judges. Whilst making no explicit reference to public policy, Cardozo uses language which is very reminiscent of Winfield's definition of public policy, as well as comments on the provisions of the civil law codes. Cardozo says that the judge is faced with a "fourfold division of the forces to be obeyed and the methods to be applied." [90] This division is comprised of logic, history, custom and:-

> " . . . the power of justice, morals and social welfare, the *mores* of the day . . ." [91] (original emphasis)

As noted, this is quite consistent with the approach of commentators and courts in both the common and civil law systems.

It might also be noted that both the United States *Uniform Commercial Code* ("UCC") and the Restatement make references to "good faith." UCC §1-203 provides that every contract or duty within UCC imposes an "obligation of good faith in its performance or enforcement." The Restatement provides that every contract imposes an "obligation of good faith and fair dealing in its performance and its enforcement." (§1-205).

European and United States parties – wider obligations?

Parties to agreements governed by civil law codes or the United States Uniform Commercial Code consequently seem to have wider duties than those whose obligations arise within the common law, although public policy is relevant in both systems. In the former, *ordre public* is formally provided for in the codes; in the latter, this is not the case, but it nevertheless exists as an essential component of the law.

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90 Cardozo, *The Growth of the Law*, Greenwood Press, 1925, at 61.

91 Cardozo, op cit, at 62.

The wider duties lie in the doctrine of good faith. Good faith is not unknown in the common law, however. Contracting parties can, for instance, impose on themselves a duty to negotiate or perform other obligations in good faith. [92] In New South Wales, the Court of Appeal has gone as far as to say that a duty of good faith (as to both contractual performance and the exercise of contractual rights) may be imposed by implication upon parties to a contract. [93]

The consequence that parties going to arbitration are required to act in good faith is discussed below in this Chapter.

Facets of public policy

It is now possible to identify a number of aspects of public policy:-

- Public policy is the broadly based guiding force for judicial legislation.

- In applying public policy, reference is made to general moral and social considerations valid at the relevant time.

- It is the interests of the community as a whole which are protected.

- There is a duty on judges to ascertain and apply public policy. Whilst public policy might not be readily apparent in some cases, this does not relieve the necessity for inquiry and application.

Public policy and legal philosophy

It has been seen that public policy involves relying on moral principle of the highest order. As well, it involves taking into consideration the interests of the whole of the

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92 For a discussion of the meaning of good faith in contract negotiations and performance, see Einstein J in *Aiton v Transfield* NSWSC 996 (1 October 1999).

93 *Renard Constructions (ME) Pty Limited V Minister for Public Works* (1992) 26 NSWLR 234; *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349 and *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187.

community. Both of these factors accord with important aspects of legal philosophy, particularly those deriving from natural law thinking.

(a) aspiration

Fuller has shown that law must aspire toward principle and morality. [94] Fuller argues that law has an inner morality, which embraces both duty and aspiration. [95] If one imagines a scale, the morality of duty lies at the bottom of that scale. The morality of duty encompasses "basic" matters which might be regarded as forbearances towards others (or social demands).

Moving up Fuller's scale, a dividing line appears, duty "leaves off . . . " and ". . . the challenge of excellence begins." [96] In order to go further, however, it is not necessary to know (or have a picture of) what is perfectly good. It is a mistake to think that standards cannot be imposed, unless we have a clear picture of what is ideal. [97] What must happen is that society must recognise what is unsuitable:-

> "We can, for example, know what is plainly unjust without committing ourselves to declare with finality what perfect justice would be like." [98]

The fact that there is no "perfect vision", no precise formula, does not prevent positions being taken on certain issues and behaviour, such positions being based on general moral values. As noted above, the language of Pollock CB in *Egerton v Brownlow* was very broad - the disposition in question was void if it was "against the public good", or was "repugnant to the State."

That the moral content of the law is no less forceful because it may be based on generalities is echoed by Cardozo:-

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94 Fuller, *The Morality of Law*, Revised Edition, Yale University Press, 1964, at 41-44.
95 Fuller, op cit, at 42.
96 ibid, and at 9.
97 Fuller, op cit, at 10.
98 Fuller, op cit, at 12.

> "The genesis, the growth, the function and the end of law - the terms seem general and abstract, too far dissevered from realities, raised too high above the ground . . .
>
> But believe me, it is not so. It is these generalities and abstractions that give direction to legal thinking . . .". [99]

The application of general moral principles is at the heart of public policy. This mirrors Fuller's concept of the search for the best (or the most appropriate) moral standards in applying the law.

(b) universality and duty

Public policy should reflect the interests of the whole of the community. There should be universality. This is the basis of Kant's categorical imperative. First , however, Kant saw duty as underpinning all human interaction. Duty provides the whole basis of morality:-

> " . . . all the morality of actions is placed in their necessity *from duty* and from respect for the law, not from love and liking what which the actions are to produce . . ." [100] (original emphasis)

The morality of all actions is found in respect for the law. Kant stated that it is important to distinguish between acting *in conformity with* duty and acting *from* duty. The latter involves acting "for the sake of the law alone", ie, acting for the sake of morality. [101] Duty, based on morality, consequently provides the motive underlying all action. Moreover, duty can only be expressed in categorical imperatives:-

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99 Cardozo, op cit, at 25.

100 Kant, *Critique of Practical Reason,* translated by Gregor, Cambridge University Press, 1997, at 69, 70.

101 Kant, op cit, at 70.

> " . . . if duty is a conception that is to have significance and real legislative authority for our actions, then such duty can be expressed only in categorical imperatives . . ." [102]

For this to be possible, however, there must be a general application:-

> " . . . if I think of a categorical imperative, I know immediately what it contains. For since, besides the law, the imperative contains only the necessity that the maxim should accord with this law, while the law contains no condition to restrict it, there remains nothing but the universality of a law as such with which the maxim of the action should conform . . . Hence there is only one categorical imperative and it is this: Act only according to that maxim whereby you can at the same time will that it should become a universal law . . . Act if the maxim of your action were to become through your will a universal law of nature." [103]

All actions must be guided by this principle, which has been summarised as "we should do as we would be done by." [104]

There are, it is submitted, similarities between the application of public policy and the categorical imperative. Both involve universality and duty. With the former, public policy is imposed for the whole community protecting universal interests. With the latter, public policy can be expressed in terms of duty:-

> "The law will not permit anything which has a tendency to be injurious to the interests of society . . . *In truth, what is denominated public policy is the obligation to perform all the duties which men owe to society*; and anything having a tendency to operate in opposition to that obligation is void." [105] (emphasis added).

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102 Kant, *Grounding for the Metaphysics of Morals*, translated by Ellington, Hackett Publishing, 1981, at 33.

103 Kant, op cit, at 29 and 30.

104 Scruton, *Kant A Very Short Introduction*, Oxford University Press, Revised Edition, 2001, at 86.

105 Bethell (Solicitor-General), in submissions in *Egerton v Brownlow*, op cit, at 371.

Public policy is mostly applied in the negative (ie, parties will be prevented from doing something) but this can be seen in terms of duty - ie, there is a duty not to engage in immoral behaviour. Public policy is therefore based, it could be argued, on duty. If a duty is breached by parties to a contract, there is a corresponding duty imposed on the courts and arbitrators not to permit the parties to benefit from their immoral or illegal activities.

Kant's principles, as summarised above, are also important in another sense. Party autonomy is an important facet of commercial arbitration. Parties are allowed the freedom to select their arbitrators, the venue, the procedure, the proper law and so on. The obligation imposed on European and United States parties to act in good faith (which must involve "doing as we would be done by"), should be strictly observed by parties who are allowed such autonomy.

Whilst this might not be so readily accepted in common law jurisdictions, it is submitted that a specific duty to act in good faith would act as a check on parties abusing the freedoms enjoyed under arbitration processes. As Priestly JA of the New South Wales Court of Appeal noted in *Renard Constructions (ME) Pty Ltd v Minister for Public Works* in relation to the duty to act in good faith:-

> " . . . there has been little if anything to indicate that recognition of the obligation has caused any significant difficulty in the operation of contract law in the United States." [106]

The obligation to act in good faith is something which could be monitored under public policy. [107] As noted above, the New South Wales Court of Appeal has stated on more than one occasion that a duty to act in good faith may be imposed by implication on parties to a contract. [108]

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106 op cit, at 267, 268.

107 This is discussed further in Chapter XII.

108 see n.92 in this Chapter.

Public policy and private international law

(a) Lauterpacht J on the importance of public policy in private international law

The New York Convention is, of course, an instrument of private international law. The importance of the role of public policy in private international law was considered and expounded by Lauterpacht J in *Case Concerning the Application of the Convention of 1902 Governing the Guardianship of Infants (Netherlands v Sweden)* ("Guardianship Case"). [109] The case concerned the application of the *Convention on the Guardianship of Infants* ("Guardianship Convention"), which had been adopted by both The Netherlands and Sweden.

The Guardianship Convention provided that the law applicable to minors was that of the infant's nationality.

B was an infant of Dutch nationality, resident in Sweden. She was in the custody of her mother, who passed away. B's father, resident in Holland, took steps in The Netherlands to assert a right of guardianship over her. The Swedish authorities, however, purported to exercise control over B via Swedish domestic laws relating to "protective upbringing" and appointed a *god man* of her. The case went through several stages and finally came before the PICJ.

The majority of the Court found that Sweden's domestic laws could apply to B, as such laws were not necessarily inconsistent with the Guardianship Convention.

Lauterpacht J also held that Swedish law applied to B, but for different reasons. His Honour firstly made a number of observations regarding the Guardianship Convention. It was a public international law statute that had as its topic a subject of private international law. In such circumstances, it fell to be interpreted as any other treaty, in light of the principles governing the interpretation of treaties in public international law. Any interpretation, however, must take into account the fact that the subject matter was a law in the sphere of private international law.

Unlike the majority, Lauterpacht J thought that there was indeed a conflict between the domestic laws of Sweden and the Guardianship Convention. Both were essentially about the same subjects. Sweden, however, was entitled to diverge from the Guardianship Convention, under a public policy exception, which recognised that foreign law may be excluded from particular cases. [110] The right of States to apply public policy considerations is recognised as being of considerable importance and that right is formally recognised. As His Honour said:-

> " . . . the recognition of the part of *ordre public* must be regarded as a general principle of law in the field of private international law." [111]

The question then arose as to what public policy was applicable - was it the public policy of Sweden? Lauterpacht J said that the public policy of Sweden could not provide the exclusive standard - the content of public policy must be determined in the same way as any other general principle of law in the sense of Article 38 of the Statute (of the PICJ), by reference to the practice and experience of the municipal law of civilised nations in that field. [112]

His Honour then made observations on the application of public policy. It was submitted by The Netherlands that public policy ought to be interpreted restrictively or refused recognition altogether. This was because its application caused uncertainty and confusion. [113]

Lauterpacht J stated that whilst there was "some substance" in these considerations, this was not decisive. As His Honour had noted, the ability to rely on public policy was a general principle of international law; but the principle was even more important than that:-

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109 International Law Reports, Volume 25 (1958 - I), 242.
110 at p.268.
111 ibid.
112 at p.269.
113 at p.270.

> " . . . it is part and parcel of the entire doctrine of and practice of private international law almost from its very inception; *the two are inseparable*, not only as a matter of history but also of necessity . . ." [114] (emphasis added).

The reason for this is that private international law makes possible the application of foreign laws within States.

Lauterpacht J describes it in terms of a "safety valve" - the State needs a "safety valve" so that its courts might, if thought necessary, decline to apply a particular foreign law. This goes to the very nature of the State - it is built on legal, moral and political conceptions which it must be able to protect. [115] It is the existence of this safety valve which makes private international law possible. [116]

As it is clear from earlier references in this Chapter that public policy is part of the law, it must follow that public policy is part of private international law. (The question of "international" public policy will be discussed below in this Chapter.)

(b) Lauterpacht J - limitations on the application of public policy

His Honour also suggested that the application of public policy in private international law was subject to reasonable limitations and any concerns over its application could be alleviated by the existence of international remedies of judicial control and review. This was necessary, however, only where the treaty or convention in question was silent as to the public policy exception. In such cases, States could not reserve a unilateral right to determine whether the exception applied. The State deciding to invoke the public policy exception ought to consent to an impartial review of its decision. [117]

No such question arises under either the New York Convention or the UNCITRAL Model Law as both instruments expressly recognise that participating States may apply a public policy exception in refusing to recognise or enforce awards.

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114 ibid.
115 ibid.
116 at p.271
117 at p.269.

The application of public policy by arbitrators

Not only courts, but arbitrators also, must apply public policy where necessary. Kirry states that:-

> " . . . public policy rules are now regarded as included in the rules of law that arbitrators must apply in resolving the disputes that are submitted to them." [118]

A contrary view is that public policy might have little place in commercial arbitration. In comparing the arbitrator's role with that of a judge, Mayer considers what an arbitrator's duties might be – the author says that it could be argued that:-

> "(As) (h)e was not appointed by the state but by the parties . . . an arbitrator is not the guardian of public policy . . . his duties are towards the parties only . . he must confine himself to the determination of disputes involving private interests." [119]

To this might be added that the only parties with an interest in the outcome are the disputants. Similar (narrow) considerations might apply to the parties' advocates. All that they are required to do is advance their clients' interests. Contrast this with court proceedings which are (except in rare circumstances) matters of public record. Judges and advocates have duties stretching beyond the immediacy of individual matters.

Mayer dismisses this line of thought:-

> "It would be most unsound for international arbitrators to adopt a stance of general indifference as regards general interests protected by states. The very

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118 Kirry, "Arbitrability: Current Trends in Europe", *Arbitration International*, 1996, Volume 12, Number 4, 373, at 378.

119 Mayer, "Reflections on the International Arbitrator's Duty to Apply the Law", *Arbitration International*. Volume 17, Number 3, London Court of International Arbitration, 2001, 235, at 241 and 246.

> survival of arbitration as a means of dispute resolution could be undermined as a result." [120]

This (pragmatic) reasoning is undoubtedly correct. Arbitration cannot function credibly unless arbitrators recognise and apply public policy.

Mayer does also look to high principle when suggesting where the duties of arbitrators lie:-

> " . . . the law has many positive aspects . . . it is neutral and predictable; it guards against arbitrariness and is reassuring for the parties; *it takes into account the general interests of the community* . . . an arbitrator should consider that it is his duty, not a legal but a professional one, to comply with the law . . . ". [121] (emphasis added)

The issue might then be whether the arbitrator's duty is a legal one, or a professional one. It is suggested that the necessity for arbitrators to consider and apply public policy ought to be based on matters of principle, rather than more pragmatic concerns.

As public policy is part of the law, it therefore becomes the arbitrator's duty to apply public policy. As arbitrators adjudicate on the rights of parties, they must call upon *all* facets of the law.

Further, when an award is made and the losing party does not conform with it, the apparatus of the courts is usually available to the winning side. In this manner, awards are elevated to a status equivalent to that of judgments. All the weight of public enforcement processes comes to the assistance of the favoured party. Public institutions may become tainted by facilitating the enforcement of an award where the underlying contract may offend public policy because, eg, it is for an legal or immoral purpose.

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120 Mayer, op cit, at 247.

121 ibid. It is suggested that Mayer's remarks are universal, as public policy in the common law is also based on the same considerations as it is in the civil law.

It follows that the public interest requires that some supervision take place:-

> "Law enforcement is no longer a private matter in any civilized community. If, acting through its agents, public authority is to enforce arbitration awards, public authority must also be in a position to check on the foundations and limitations of arbitration." [122]

Diplock J (as he then was) noted in *London Export Corporation Limited v Jubilee Coffee Roasting Co Limited* [123]:-

> " . . . an arbitrator's award, unless set aside, entitles the beneficiary to call upon the executive power of the State to enforce it and it is the function of the court to see that the executive power is not abused." [124]

This goes only so far - of course, the integrity of public institutions must be protected, but public policy must also be applied in light of the considerations referred to above - the character of the community, its social, moral and economic interests, must also be protected.

Can public policy go beyond the "parochial" or "domestic"? Is there an international public policy?

It is clear that international public policy exists, although some clarification must be made as to what is meant by "international" public policy and what relevance this has for the New York Convention. Under Article V.2(b) of the Convention, recognition or enforcement of an award may be refused where a competent authority of the

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122 Schwab, "Legal Foundations and Limitations of Arbitration Procedures in the US and Germany", in Sanders (ed), *International Arbitration Liber Amoricum for Martin Domke*, Martinus Nijhoff, 1967, 301, at 307.

123 [1958] 1 WLR 271.

124 op cit, at 278.

country where the award is sought to be enforced if that authority finds that enforcement would be contrary to the public policy of *that country*. It is generally recognised that this refers, not to the purely domestic public policy of States, but to their international public policy [125] or, as Lew puts it, "national international" public policy. [126]

Public policy, however, also exists at a higher level, which Lew describes as "truly international" or "transnational" public policy, which is not concerned with national influences, but which reflects:-

> " . . . only the fundamental standards of the international community . . . and is developed from common standards of national policies, as well as fundamental concepts which have been embodied in international conventions or other international instruments." [127]

Lew gives as examples of international public policy the maintenance of human rights, preventing terrorism, avoiding abuses by multi-national entities and eliminating bribery and corruption. [128]

Gaillard and Savage also provide examples which they consider to fall within international public policy - corruption, customs offences, breaches of embargoes, antitrust violations and drug trafficking. [129]

In a formal context, international public policy is recognised in the French *Code Civil*, which, as noted in Chapter III, provides that arbitral awards may not be enforced if they are contrary to international public policy.

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125 Gaillard and Savage (eds) *Fouchard Gaillard Goldman on International Commercial Arbitration*, Kluwer Law International, 1999, at paragraph 1710.

126 Lew, in Lew (ed), *Contemporary Problems in International Arbitration*, Martinus Nijhoff, 1987, at 83.

127 ibid.

128 ibid.

129 op cit, at paragraph 1521.

Lew notes several ICC cases in which arbitrators applied international public policy, where parties did not raise the issues themselves. [130] In England, international public policy was applied by the House of Lords in the decision of *Kuwait Airways Corpn v Iraqi Airways Co (Nos 4 and 5)*. [131] In that case, aircraft belonging to the Kuwaiti plaintiff had been seized by Iraq during the Iraqi invasion of Kuwait in 1990. After the seizure, the Iraqi Revolutionary Command Council passed a number of resolutions purporting to annex the State of Kuwait and also to transfer property belonging to Kuwaiti citizens. Those resolutions included a resolution ("Resolution 369") which, *inter alia*, purported to dissolve the plaintiff and transferred all its assets to the defendant.

The UN Security Council passed a resolution which condemned the invasion as a breach of international peace. [132] The Security Council then called upon Iraq to rescind its annexation of Kuwait and to return all Kuwaiti property seized by Iraq. [133] The plaintiff issued a writ in the English Commercial Court seeking the delivery up of the aircraft. In answer to the claim, the defendant argued *inter alia* that the English courts could not adjudicate on acts performed by a foreign sovereign State. This was rejected by the majority of the House of Lords, on the basis of public policy.

During the course of his speech, Lord Steyn said:-

> "In recent years, particularly as a result of French scholarship, principles of international public policy (l'ordre public véritablement international) have been developed in relation to subjects such as traffic in drugs, traffic in weapons, terrorism and so forth . . .

130 Lew, *Contemporary Problems*, op cit, at 83-84.
131 [2002] 2 AC 883.
132 Security Council Resolution 660 (1990), 2 August 1990.
133 Security Council Resolution 686 (1991), 2 March 1991.

> The public policy condemning Iraq's flagrant breaches of public international law *is yet another illustration of such a truly international public policy* in action." [134] (emphasis added).

Lord Hope also spoke of the international character of the issues involved. His Lordship noted that in order to attract the jurisdiction of the courts of the United Kingdom, under the relevant common law rule existing at the time of the commission of the acts in quotes (the double actionability rule), the plaintiffs had to establish that an action was available to them under both the law of the forum and the law where the alleged torts took place. [135] The defendants had asserted, however, that Iraqi law permitted them to do what they had done. The plaintiffs action would fail if double actionability did not apply.

Lord Hope referred to an article [136] in which Mann had stated that municipal courts could not, under conflict of law rules, apply a foreign law where such law resulted from an international delinquency. Consequently, a public policy exception to the general rule which required double actionability might be invoked. It was not sufficient, however, that the Iraqi Resolution 369 was contrary to English public policy alone. The public policy exception to the general rule was not of a parochial or domestic nature:-

> "It is based on the Charter of the United Nations . . .
>
> The whole basis upon which RCC Resolution 369 proceeded was the subject of universal international condemnation. It was one of a series of acts which were performed in clear breach of international law. I would hold therefore that, *as the public policy objection is truly international in character*, there is a sound basis in principle for severing this part of the lex loci delicti and disregarding entirely any legal effects which would be given under Iraqi law to

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134 op cit, at 1099. His Lordship referred to Gaillard and Savage - ibid.

135 op cit, at 1112.

136 Mann, "International Delinquencies before Municipal Courts", (1954) 70 Law Quarterly

> the resolution which purported to vest the title to KAC's aircraft in IAC." [137] (emphasis added).

It is therefore clear that "international" public policy exists and is continuing to develop. The fundamental criteria appears to be true "internationality". In the *Kuwait Airways* case, it is perhaps easy to see that the fact of the Iraqi invasion (and Iraq's subsequent acts of conversion and transfer of property) was a "truly international" matter. The UN Security Council determined that there had been a breach of international peace and Iraq's actions were the subject of universal condemnation. Examples as clear as this will not always present themselves. (There is further discussion on the possible content and sources of international public policy in Chapter XII).

The ramifications of the House of Lords decision seem clear, however. As courts have a duty to apply public policy, they must also apply (where necessary) international public policy. International public is part of public policy. Naturally, this must also apply to arbitrators, as they also have a clear duty to apply public policy. This becomes vitally significant in international transactions. As Lew states, arbitrators are:-

> " . . . the private guardians of international commercial transactions . . . " [138]

As such, arbitrators are the frontline check to bar the enforcement of contracts which are illegal or immoral.

Review, 181, at 203.

137 op cit, at 1116.

138 Lew, *Contemporary Problems*, op cit, at 85.

Which public policy is to be applied?

The question arises as to what happens when public policy becomes "cumulative." [139] An arbitrator may be faced with competing public policies. It is suggested that the appropriate approach is to perform a balancing act:-

> "The arbitrator will then use his best efforts to avoid a breach of the international public policy of the state where the arbitration takes place, and if possible also of the state where the recognition of the award will clearly be sought." [140]

Rubino-Sammartano states that the relevant "connecting factors" are to be evaluated just as in any decision on what is the applicable law. [141] Lew says much the same thing - arbitrators must "be mindful" of the existence of the two types of public policy. [142] In so doing, arbitrators and courts may look beyond the law of the forum and the law of the contract. Rubino-Sammartano notes the English House of Lords decision, *Regazzoni v K C Sethia (1944) Limited.* [143] The contract called for the respondents (an English company) to ship jute from India to Genoa, from where it was then to be shipped to South Africa. The contract was governed by English law. Indian law, because of South Africa's apartheid policies, prohibited both the direct and indirect shipment of goods from India to South Africa.

The jute was not delivered. The appellants sued the respondents in the United Kingdom. The House of Lords refused performance of the contract, as enforcement would have violated the law of a friendly country. The parties were aware that the contract could not be fulfilled without a breach of Indian law. That was enough to render the contract unenforceable in the United Kingdom. [144] Rubino-Sammartano describes this decision as being one of the "first signs" of "transnational public

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139 Rubino-Sammartano, at 533.
140 ibid.
141 ibid.
142 Lew, *Contemporary Problems*, op cit, at 83.
143 [1957] 3 All ER 286.

policy". [145] Whilst there will be circumstances where international public policy should clearly apply, it will largely be left to the arbitrators in each case to decide the most important connecting factor to determine which public policy is (the most) relevant.

International public policy and the New York Convention

The context in which public policy is directly relevant in the text of the Convention is in Article V.2(b).

In this context, Gaillard and Savage state that, notwithstanding the words of the Convention, public policy can also be "genuinely international":-

> "It is . . . clear that Article V, paragraph 2(b) refers to the host country's conception on international public policy, and not to a 'genuinely international public policy' rooted in the law of the community of nations . . . However, there is nothing to prevent each country from adopting, as part of its conception of international public policy, principles having some claim to universality, whether voluntarily or in order to satisfy its international commitments." [146]

International public policy must be recognised in the context of Article V.2(b). Consensus on international public policy exists in relation to a number of issues and consequently, both courts and arbitrators, as part of their duty to apply public policy, must take cognisance of this.

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144 see Viscount Simonds at 293-295; Lord Somervell at 297.
145 Rubino-Sammartano, op cit, at 534.
146 Gaillard and Savage (eds), op cit, paragraph 1712.

For the reasons set out in this Chapter, public policy considerations are essential to the functioning of commercial arbitration.

CHAPTER V

PUBLIC POLICY NOW FAVOURS ARBITRATION

> "*They had great jealousy of arbitrations . . . they said that . . . it was contrary to the policy of the law.*" [1]

> "*The concept of arbitrability . . . relates to public policy limitations upon arbitration.*" [2]

Evolution of attitudes

Initially, courts were reluctant to permit parties to even arbitrate. That position has changed. Public policy now dictates that arbitration is a desirable form of dispute resolution and should be promoted.

Legislatures also initially demonstrated a rigid approach to commercial arbitration, by, eg, imposing strict controls on processes, or prohibiting access to arbitration in respect of particular subject matters.

Along with the judicial exercise of public policy considerations, this has changed:-

> "Legislatures have taken the lead in promoting and encouraging commercial arbitration and modern commercial arbitration in the United States is a creature of statute." [3]

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1 *Scott v Avery* [1843-1860] All ER Reprints, 1, at 7, per Lord Campbell.

2 Redfern and Hunter, Second Edition, op cit, at 137. Sometimes, the expression arbitrability may be used in the context of whether the subject matter of the arbitration falls within the particular arbitration clause; otherwise, it relates to the constraints placed on parties by courts and legislators, as to whether certain subject matters are suitable for arbitration. It is the latter meaning which is relevant for the purposes of the discussion which follows.

This is true of most Western jurisdictions. One of the principal features of the evolution is that generally, court intervention in arbitral processes is now kept to a minimum.

Arbitrability, nonetheless, remains an issue, particularly where there may be national interests involved – ie, the desire of States (particularly developing countries) to retain control over aspects of economic policy and development. It may be seen as imperative in many cases to retain control over certain industries. Where the wellbeing of a particular industry is perceived as essential to the public interest, then disputes ought not be resolved in private fora:-

> "The doctrine of arbitrability rests on the simple proposition that arbitration, being based on the agreement of the parties for the disposal of a dispute between themselves cannot be the means for the disposal of a dispute which involves public interests or the interests of third parties." [4]

The availability of access to arbitration consequently reflects prevailing interests, goals and values – as does any public policy position.

It is proposed to demonstrate by way of example the move in more recent times towards favouring arbitration, by looking at developments in particular States. It will be seen that both legislation and judicial attitudes have evolved.

The jurisdictions which will be referred to are – Australia, France Switzerland, the United Kingdom, the United States and Australia.

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3 Shell, "Res Judicata and Collateral Estoppel Effects of Commercial Arbitration", *UCLA Law Review* April 1988, 623, at 635.

4 Sornarajah, "The UNCITRAL Model Law: A Third World Viewpoint" (1989) 6 *Journal of International Arbitration*, 7, at 15.

United Kingdom

(a) Submissions were revocable

English Courts were for a long time reluctant to allow much latitude to parties seeking arbitration.

Vynior's case was referred to earlier. [5] Ehrenzweig refers to this decision as being regarded as the "fountainhead of hostile judicial attitudes against arbitration." [6] Lord Coke had stated that a submission to arbitration was "countermandable", in much the same fashion as a will could be revoked. [7]

In 1856, in the landmark decision of *Scott v Avery* [8], where an agreement to arbitrate was upheld, Lord Campbell spoke of the "very great inclination" of the courts to "throw obstacles in the way of arbitration." [9] This, His Lordship continued, was due to the fact that formerly, the moneys paid to judges as emoluments depended "almost entirely" upon the amount of fees they collected. Judges had no fixed salary. As a consequence, the various courts had an interest in having matters litigated and there was great competition between them. His Lordship said about the courts:-

> "They had great jealousy of arbitrations, whereby Westminster Hall was robbed of those cases which came neither into the Queen's Bench, nor the Common Pleas, nor the Exchequer. Therefore, they said that the courts ought not to be ousted of their jurisdiction and that it was contrary to the policy of the law." [10]

Lord Campbell then stated that he believed that the true position regarding ouster of jurisdiction was as Lord Coke had held, being that, where a court action was indispensable, such as in redress for waste, it was only then that the jurisdiction of the

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5 see Chapter I.
6 Ehrenzweig, *A Treatise on the Conflict of Laws*, West Publishing Co, 1962, at 156.
7 Ehrenzweig, ibid; *Vynior's* case, op cit.
8 op cit.
9 at 7.
10 ibid.

courts could not be ousted. [11] In the instant case, the contract merely provided that there should be arbitration as a condition precedent to bringing an action. The creation of the condition precedent clearly did not oust the court's jurisdiction.

From this, it might be seen that antipathy to arbitration, as demonstrated by the English Courts, was in reality based on the necessity to ensure that as much business as possible came the way of the courts.

Sayre takes a different view. The author refers to Lord Campbell's speech in *Scott and Avery*, but diverges from Lord Campbell's views. Sayre states that the view that competition for business was the real reason behind judicial antipathy to arbitration, was accepted "without any evidence . . . in its support." [12] Sayre continues that he finds it "difficult to explain" how a distinguished judge such as Lord Campbell should have made the "assertions" he did. If the Courts had really been anxious to attract as much business as possible, then they would have declared that the provision of a bond to force arbitration was against public policy. [13]

The real reason (according to Sayre) was that the courts would not permit a party to make a submission to arbitration irrevocable, as arbitration did not provide the protections that court proceedings did. Further, when the law changed and bonds could no longer be relied upon as a mechanism to force arbitration, plaintiffs were forced to approach the courts. The courts upheld the doctrine of revocability, as the party revoking the submission could still have his or her interests protected by a court proceeding. [14]

It would seem, however, that the adoption of the principle of revocability would have had the same effect as voiding any mechanism designed to force arbitration.

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11 ibid.
12 Sayre, op cit, at 610.
13 ibid.
14 Sayre, op cit, at 609 et seq.

In a speech to the International Conference on International Commercial Arbitration in Sydney in 1999, the President of the New South Wales Court of Appeal, Justice Keith Mason, whilst noting Lord Campbell's comments in *Scott v Avery* (and the fact that His Lordship's "frank self-revelation" is omitted from later reports of the decision), also listed some further reasons for the historical judicial distrust of arbitration. These included perceived deficiencies in processes, expense, difficulties of enforcement and lack of finality. Also, arbitration, as a private process, clashed with the common law's ideal that justice ought to be administered in public. [15]

(b) The "stated case" procedure

English Courts also asserted a great deal of control over arbitration via the "stated case" procedure. Essentially, this provided that an arbitrator could (and was obliged to do so if directed by the High Court), state a special case for the High Court on any question of law arising in the course of a reference to arbitration, or on an award (or any part of an award).

These provisions had the potential to cause much delay, not only in the hearing of arbitrations, but subsequently, as the enforcement of awards was also subject to these processes.

In the Court of Appeal decision, *Halfdan Grieg & Co A/S v Sterling Coal and Navigation Corp and anor (the "Lysland")* [16], Denning MR noted:-

> "When the parties so arbitrate, it is, by our law, on the assumption that a point of law can, in a proper case, be referred to the Courts." [17]

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15 Mason P, *Changing Attitudes in the Common Law's Response to International Commercial Arbitration*, International Conference on International Commercial Arbitration, Sydney, 9 March 1999.

16 [1973] 1 QB 843.

17 op cit, at p. 862.

His Lordship continued, referring to the issue of contract construction:-

> "The Court would, of course, give great weight to the views of arbitrators and umpires upon it, but should come to its own decision." [18]

Such views ensured that the Courts exercised a good deal of control. Lord Denning's views on contract construction were perhaps exemplified in *Wickman Machine Tool Sales Limited v L Schuler AG* [19]. The respondents terminated the agreement for breach of a condition which they said entitled them to regard the agreement as having been repudiated. The appellants, as agents for the respondents, had failed to carry out a relatively small number of client visits as required under the agreement. That requirement was stipulated as a condition. The arbitrator found that the respondents were not, on the "true construction" of the agreement, entitled to terminate. Mocatta J, in the High Court, reversed the arbitrator's finding. The appellants went to the Court of Appeal, which, by majority, allowed the appeal, holding that the arbitrator's reasoning was correct.

Denning MR, whilst noting that the evidence of the parties as to their intention "was not helpful", stated that the Court should not go by "supposed common intent" in any event, but on a reasonable construction of the wording used. [20]

In *Halfdan Grieg*, the arbitrator had refused to state a case on the award. Denning MR laid down certain guidelines for arbitrators to observe when requested to state a case – the point of law had to be "real and substantial"; it had to be "clean cut", in that a question of fact could not be "dressed up" as a point of law; and, it had to be of such importance that its resolution was necessary for the proper determination of the case. When the prerequisites were met, then, as Denning MR said:-

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18 op cit, at p. 863.
19 [1972] 2 All ER 1173.

" . . . the arbitrator or umpire *should* state a case." [21] (emphasis added)

Arbitrators were in something of a bind. Even if they did not state a case, a party could still approach the court seeking orders compelling the arbitrator to do so. Further, this was not limited to questions of general application. [22] In practice, all that had to be found was a point of law which it might be argued had a bearing on the decision.

Consequently, the parties could approach the court at almost any stage of the arbitral process.

In 1978, the *Commercial Court Committee Report on Arbitration* was presented to the United Kingdom Parliament. The Committee noted, *inter alia*, that most systems of law adopted the philosophy that parties, having chosen their tribunal, must accept its decisions with any consequent faults. [23] The Committee criticised the stated case procedure, noting that judicial review caused delay and expense.

Parliament accepted these criticisms and on 31 August 1979, the *Arbitration Act* 1979 came into effect. One of the Act's more significant features was the repeal of s21 of the 1950 *Arbitration Act*. S1(1) of the 1979 legislation provided that an appeal should not lie to the High Court for "errors of fact or law on the face of the record." A right of appeal on any question of law was granted under s1(4), but this was subject to the Court being satisfied that, having regard to all the circumstances, the determination of the point of law could substantially affect the rights of one of the parties. Leave could also be granted conditionally.

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20 op cit, at 1179. His Lordship's words might be seen as striking at the idea of party autonomy, by substituting the Court's view for the intention of the parties. An appeal was dismissed by the House of Lords – *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235.

21 at 862.

22 ibid.

23 Paragraph 4.

Unfortunately, the new provisions also created difficulties of their own. The courts still took a very liberal approach in allowing appeals. In *Schiffahrtsagentur Hamburg Middle East Line GmbH v Virtue Shipping Corporation Monrovia (the "Oinoussian Virtue")* [24], Robert Goff J said that, in considering an appeal, the only limitation placed on the question of law to be decided was that it must substantially affect the rights of one of the parties. This seems not too far removed from Lord Denning's guidelines for stated cases in *Halfdan Grieg*, the problems with which the new provisions were meant to abolish.

In *Pioneer Shipping Limited and anor v BTP Tioxide Limited* [25], however, the House of Lords decided that some parameters ought to be placed around the rights of appeal.

In his speech (with which the remainder of their Lordships agreed), Lord Diplock said that this particular matter should not have been allowed to progress so far through the Courts. The trial judge had not, in the instant case, paid sufficient regard to the general discretion to "*refuse* leave absolutely" to appeal. [26] (original emphasis).

His Lordship laid down what became known as the "*Nema*" guidelines to be utilised when considering whether to grant leave to appeal from an award. These included:-

- where the parties needed a speedy resolution, so as to know where they stood in relation to future conduct, then granting leave will be inappropriate; and

- where the question of law involved the interpretation of a "one-off" clause, then leave should not be granted unless, from a mere perusal of the award, the meaning attributed to it by the arbitrator was obviously wrong; and

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24 (1981) 1 Lloyd's Rep 533.
25 [1982] AC 724.
26 at p. 739.

- in the case of "standard" terms, however, all that was needed was a strong *prima facie* argument that the arbitrator's award was wrong.

Lord Diplock's attempts to introduce some controls over the appeal mechanism, however, were perhaps not met with overwhelming enthusiasm from Lord Denning, at least. In *Italmare Shipping Co v Ocean Tanker Co Inc* (*the "Rio Sun"*) [27], the Master of the Rolls said:-

> ". . . I feel that we must go by the guidelines set out by the House of Lords. Subject to remembering this - they are only guidelines . . . Useful as guidelines often are, nevertheless, it must be remembered that they are only guidelines. They are not barriers.
>
> . . . So let each case depend on its own circumstances." [28]

The House of Lords then revisited the *Nema* guidelines in *Antaios Compania Naviera SA v Salen Rederierna* (*"The Antaios"*) [29]. In his submissions to the Court, Saville QC (later Lord Saville of the House of Lords) said that there was "some disquiet in the city", not over the *Nema* guidelines themselves, but over the fact that there were often extensive hearings before the Courts in order to determine whether leave to appeal should be granted. [30] Lord Diplock took the opportunity to restate why the Nema guidelines had been introduced in the first place. His Lordship referred to the way in which:-

> " . . . parliamentary intention was being thwarted . . . by parties applying for leave to appeal from any award that involved a question that was even remotely arguable . . . and by some, though not all, commercial judges following a policy of granting leave in virtually all such cases . . . " [31]

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27 [1982] 1 WLR 158.
28 at p. 162.
29 [1985] AC 191.

His Lordship reaffirmed the appropriateness of the *Nema* guidelines and stated that leave to appeal should only be granted where the case:-

> " . . . called for some amplification, elucidation or adaptation to changing practices of existing guidelines . . ." [32]

The remainder of their Lordships again agreed with Lord Diplock's speech.

The passing of the *Human Rights Act* 1998 in the United Kingdom [33] has led to some reconsideration of Lord Diplock's dicta in *The Antaios*. His Lordship had also stated that, save in exceptional cases, a judge ordinarily "ought not to give reasons for a grant or a refusal . . . of leave to appeal to the High Court from an arbitral award." [34] In *North Sea Shipping Ltd v Seatrans Shipping Corp* [35], the English Court of Appeal noted the provisions of Article 6 of the *European Convention for the Protection of Human Rights and Fundamental Freedoms* 1950 (the Convention being incorporated into English Law by Schedule I of the United Kingdom *Human Rights Act* 1998). Article 6 of the Convention provides for the right to a fair hearing.

The Court of Appeal said that Article 6 now required the giving of reasons for such decisions.

Switzerland

Switzerland is another example of a jurisdiction which has moved towards a more liberal attitude regarding arbitration. As was noted in Chapter III, Switzerland amended its arbitration law in 1987. Until then, arbitration was governed by the Concordat, certain aspects of which had been the subject of some criticism. This

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30 at 197.
31 at 199.
32 at 205.
33 Schedule I of which brought into English law the *European Convention for the Protection of Human Rights and Fundamental Freedoms* 1950.
34 *The Antaios*, ibid.
35 [2002] 4 All ER 390.

criticism was levelled particularly at the grounds upon which enforcement of an award may be resisted.

Article 36 of the Concordat sets out the various grounds on which an award may be annulled by a cantonal court; sub-Article *f* provides that an award may be annulled if it is "arbitrary." An "arbitrary" award is defined as one based on findings which were "manifestly contrary to the facts", or as one which constitutes a "clear violation" of law or equity. The Swiss concept of arbitrariness has been criticised as providing an "excessively broad" standard of review [36] and as being "too ambiguous". [37]

The term "equity" in Article 36 does not refer to equitable principles such as those applying in common law jurisdictions - to do "equity" under Article 36, there must be no error of substantive law or no defects in procedure. [38] Whilst the Swiss Federal Tribunal has attempted to rein in appeals under this provision by setting guidelines, the gap between theory and practice often diverges and some cantonal courts retain a "more interventionist" approach as to what might constitute arbitrariness. [39]

As noted in Chapter III, the Concordat permitted appeals on the grounds *inter alia* that the award was "arbitrary". The *Loi federale sur le droit international privé* ("*Loi*") did not repeat this provision, narrowing the grounds for appeal.

Despite the *Loi* moving away from the previous tests, there has been, however, some criticism as to the Swiss courts willingness to allow appeals under the *Loi*. In the *Maran/Vekoma* decision [40], the Swiss Supreme Court set aside an award rendered in Geneva by an ICC arbitral panel, on the grounds that the arbitrators had misapplied contractual provisions regarding jurisdiction. The agreement had provided that

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36 Craig, "Some Trends and Developments in the Law and Practice of International Commercial Arbitration", Volume 30, *Texas International Law Review*, 1, at 33.

37 Berger, op cit, at 672.

38 Craig, Park and Paulsson, *International Chamber of Commerce Arbitration*, second edition, Oceana Publications, 1990, at 555.

39 Craig, Park and Paulsson, op cit, at 556.

40 Described as such by Friedland, in a case note, "The Swiss Supreme Court Sets Aside an ICC Award", (1996) 13 *Journal of International Arbitration*, at 111.

arbitration should commence within 30 days after "it was agreed that the difference or dispute cannot be resolved by negotiation."

A dispute had arisen when Maran (the United States buyer) complained to Vekoma (the Dutch seller) about the quality of a shipment of coke. The parties met to discuss the issue, but without resolution. On 9 January 1992, Maran submitted a claim for compensation to Vekoma and requested a response by 17 January 1992. Maran also warned that if there was no response by the indicated date, it would apply for arbitration. There was no response; Maran sent a further message on 3 April 1992, to which Vekoma replied on 13 April, stating that it thought the matter was closed.

Maran commenced arbitration on 11 May 1992. Before the arbitrators, Vekoma argued that the time for commencement had expired - Maran should have commenced within 30 days of 17 January 1992, its deadline for a response to its claim. This argument was rejected by the arbitral tribunal. The tribunal held that, in the circumstances, silence did not amount to an unequivocal rejection of the claimant that as Vekoma's silence was not in good faith, it could not benefit from that. Further, the tribunal concluded that Vekoma had indeed continued to consider the matter after 17 January. [41]

On appeal, the Swiss Supreme Court agreed with Vekoma. The Court said that it was irrelevant that bad faith may have been exercised by Vekoma in not responding to Maran's claim. Maran was obliged to accept the consequences of the unilaterally imposed deadline. [42] The Court relied on Article 190.2(b) of the *Loi federale sur le droit international privé*, which provides for relief if the arbitral tribunal erroneously held that it did or did not have jurisdiction.

Friedland (a partner with Coudert Brothers, who were Maran's legal advisers) criticises the judgment on two grounds - firstly, that the Court substituted its own judgment for that of the arbitrators and secondly, that it failed to apply the parties'

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[41] Friedland, op cit, at 114.

contract. The author also says that the enactment of the new legislation was supposed to curb judicial review, by bringing to an end the re-deciding of factual issues:-

> "The distinction that the Supreme Court overlooked is that rejection by one party of a particular settlement position . . . in no way necessarily implies that negotiations have definitively failed . . . the Court unjustifiably and illogically found that rejection of a particular offer . . . showed that all settlement negotiations were ended." [43]

Whilst Friedland's firm was adviser to the losing party, it is submitted that these criticisms have some merit. With respect to the Swiss Supreme Court, the finding that all negotiations had failed merely because Vekoma had not responded to Maran's claim, seems to have been somewhat harsh.

For one party in a commercial dispute to set a deadline for a response to an offer (and to threaten proceedings if the offer is not accepted) is hardly unusual; and for the other party to ignore the deadline is also hardly unusual. The Court seems to have found a rather premature place in time to have drawn the line. It is also generally recognised that it is competent for an arbitral panel to determine whether it has jurisdiction to hear a dispute. As Craig, Park and Paulsson note:-

> " . . . the court does not decide whether a Request for Arbitration is time-barred by virtue of a statute of limitation or another form of prescription. Such an issue would be determined by the arbitral tribunal under the law it deems applicable." [44]

If it continues to be held that the effect of Article 190.2(b) is to circumscribe the jurisdiction of arbitrators, it is understandable that this would cause some disquiet

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42 ibid.
43 Friedland, op cit, at 115.
44 Craig, Park and Paulsson, op cit, at 186.

amongst parties and practitioners hoping for a regime which seemed to promise less court intervention than in the past.

It should also be noted that Switzerland now takes a broad approach to what type of matters might be considered arbitrable. Under Article 177 of the *Loi federale sur le droit international privé*, any claim having a "financial value" is arbitrable. There are no "value judgments" restrictions on whether certain kinds of claims are best left to Courts.

France

Kirry describes how, gradually, judicial opposition to arbitration has softened. [45]

Under the French Civil Code, matters "related to public policy" could not be referred to arbitration. The courts' attitude to this provision began to change in 1950, when the *Cour de Cassation* held that the fact that the subject matter of a dispute was subject to public policy rules, did not of itself prevent the dispute being referred to arbitration. [46] This policy change was later extended to international arbitrations, but the courts still imposed some restraints - an actual violation of public policy rules remained non-arbitrable.

This position, however, was seen as illogical, as, in essence, arbitrators had to decide whether public policy rules had been breached in order to decide whether arbitration was possible. Disputes were virtually decided via the consideration of this threshold issue. [47]

The French courts adopted their present approach via two decisions - the first in 1991, the second in 1993. [48] In *Ganz*, it was claimed that the carrying out of a

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45 Kirry, op cit, at 373.
46 Kirry, op cit, at 375.
47 ibid, and 376.
48 Kirry refers to these as the *Ganz* and *Labinal* decisions respectively.

corporate reorganisation was, in the circumstances, fraud, and consequently in breach of international public policy. It followed, the argument continued, that the arbitration agreement was void. The Paris Court of Appeal held that the dispute was arbitrable. In *Labinal*, it was alleged that there had been unfair competition, and, as competition law is a question of public policy, only the courts had jurisdiction to hear the matter. This was also rejected by the Paris Court of Appeal.

Kirry also notes that certain European countries have adopted a "relaxed notion" of public policy, which is now said to cover only "fundamental principles", or, following the United States' authorities, the "most basic notions of morality and justice." [49] He concludes that very few references to arbitration would offend such notions. [50]

It would seem that matters which offend fundamental concepts of morality and justice would be more likely to arise in relation to enforcement, rather than in considering whether a dispute was arbitrable - although, it is of course possible that allowing a particular dispute to be submitted would offend against morality and justice. In such a case, it seems likely that such a dispute would also be non-justiciable before a court.

Kirry also discusses the issue of finding the applicable law in considering arbitrability. He notes the "marked tendency" to now approach arbitrability "on the basis of substantive rules." [51] Applying the doctrine of separability, the arbitration agreement is independent of the other parts of the contract. The arbitration agreement is the "procedural clause" which concerns only the settlement of disputes and has nothing to do with the parties rights and obligations, which are found in other parts of the contract. [52]

In this context, a conflict of laws approach is inappropriate. In relation to considerations of the place of arbitration, the parties chose the place of arbitration for

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49 Kirry, op cit, at 378.
50 ibid.
51 op cit, at 374.

convenience, or for reasons associated with perceptions of neutrality. This is of little assistance in determining what law might apply. Further, considering the law of the possible place of enforcement also presents difficulties, as, firstly, this amounts to a pre-determination of the outcome of the case and secondly, in any event, there may be more than one potential place of enforcement. [53]

What the courts have done is look to a subjective test for arbitrability – the capacity of and intention of the parties in entering arbitration agreements. Kirry then refers to the *Dalico* case, in which the *Cour de Cassation* applied the separability doctrine and said that the validity of the arbitration agreement was to be assessed in light of the intention of the parties, subject to mandatory rules of French law and international public policy. [54] The *Cour de Cassation* took the view that the validity of the arbitration agreement was to be established *only* against mandatory principles of law and international public policy. [55]

United States

(a) liberalising the approach to arbitrability

Judicial antipathy towards arbitration was also noticeable in the United States.

In 1920, the State of New York introduced legislation (the *New York Arbitration Law*) which became the forerunner for the Federal legislation (the *Federal Arbitration Act*) introduced in 1925. The Supreme Court of the United States noted that the introduction of the *Federal Arbitration Act* had reversed centuries of judicial hostility to arbitration. [56]

The Supreme Court had historically regarded certain types of statutory remedies as being unsuitable for arbitration. This was due to the policy perception that certain

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52 op cit, at 380.
53 ibid, et seq.
54 op cit, at 385.
55 ibid.
56 *Scherk v Alberto- Culver*, 417 US 506 (1974), at 510.

matters were exclusively the preserve of the Courts. In this way, arbitrability, or lack of it, determined which causes might be referred to arbitration; public policy greatly curtailed reference to arbitration:-

> "US courts traditionally awarded nominal damages for breaches of arbitration agreements. Like English courts, American judges refused to grant specific enforcement of arbitration agreements . . . This grudging approach towards arbitration agreements reflected a variety of factors . . . " [57]

The opinion of the majority in *Wilko v Swan* [58] is perhaps typical of the approach initially taken by the Supreme Court. In that case, the petitioner sued his stockbroker, alleging that he had been induced to purchase shares by the broker's false representations regarding the value of the shares. The contract between the parties provided for the settlement of disputes by arbitration. The petitioner instigated court proceedings, however, in the District Court for the Southern District of New York, relying on the provisions of the *Securities Act* 1933.

S12(2) of the *Securities Act* provides *inter alia* that any person who sells a security on the basis of a misrepresentation, shall be liable in damages to the person purchasing the security. This section also provides that the onus of proof is reversed, with the purchaser not required to prove that he or she was not aware of the untrue statement. The *Securities Act* gives jurisdiction to any Federal or State Court to hear claims under s12(2). If a plaintiff choses a Federal Court, he or she has a choice of venue.

In answer to the proceedings in the District Court, the Respondents attempted to force the matter to arbitration. The District Court rejected the application, relying on s14 of the *Securities Act*, which provides that any agreement requiring a party to waive compliance with the *Securities Act* shall be void. The Court of Appeals for the Second Circuit (by majority) reversed the decision, holding that s14 did not preclude references to arbitration.

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57 Born, *International Commercial Arbitration in the United States*, Kluwer, 1989, at 29.

58 346 US 427 (1953).

The petitioner, assisted by the Securities and Exchange Commission (who appeared as *amicus curiae*), went to the Supreme Court. The petitioner argued that arbitration lacked the certainty that a court would provide to enforce his rights and that the agreement to arbitrate was caught by s14. The respondent countered that arbitration was merely a form of trial, in lieu of a trial at law. The ability to arbitrate merely simplified the ability to recover damages for statutory breach. [59]

The Court (the majority opinion being delivered by Reed J) noted that the reversal of the onus of proof provided plaintiffs with a "special right to recover for misrepresentation", such right "differing substantially" from common law rights. [60] His Honour continued that, as issuers and dealers in securities have better opportunities than buyers to investigate and appraise information relating to securities, Congress had placed buyers of securities on a different footing to purchasers in other situations. [61] Consequently, if a security buyer surrendered the right to bring a court action, the buyer thereby gave up more than did participants in other business transactions. [62] Such a party:-

> " . . . surrenders one of the advantages the Act gives him . . . at a time when he is less able to judge the weight of the handicap the Securities Act places upon his adversary." [63]

Reed J continued by noting that the case required subjective findings on the purpose and knowledge of an alleged violator of the law. These findings must be made by arbitrators who were "without judicial instruction on the law". As awards could be made without explanation of reasons and without a complete record of proceedings, the arbitrators' understanding of the legal expressions as set in s12(2) could not be examined. Their interpretations of the law would not be scrutinised. As the remedial

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59 op cit, at 433.
60 op cit, at 431.
61 op cit, at 435.
62 ibid.
63 ibid.

provisions of the *Securities Act* required judicial process to ensure their effectiveness, Congress must have intended s14 to apply to waiver of judicial trial. [64]

Reed J also noted that there were two policies, "not easily reconcilable", involved. On the one hand:-

> "Congress had afforded participants in transactions . . . an opportunity generally to secure prompt, economical and adequate solution of controversies through arbitration if the parties are willing to accept less certainty of legally correct adjustment. On the other hand, it has enacted the Securities Act to protect the rights of investors and has forbidden a waiver of any of those rights." [65]

Reed J decided that the intention of Congress was "better carried out" by holding any waiver of rights invalid. [66]

In dissent, Frankfurter J stated that there was nothing before the Court which would indicate that the arbitral system would not:-

> " . . . afford the plaintiff the rights to which he is entitled." [67]

Further, His Honour noted, in New York, there were 4,400 arbitrators who were members of the American Arbitration Association. Of these, 1,275 were lawyers. [68]

In the 1974 decision of *Scherk v Alberto-Culver* [69], the United Sates Supreme Court distinguished *Wilko v Swan*. In *Scherk*, an action was brought under the *Securities Exchange Act* 1934, alleging misrepresentations over trade marks. Like the *Securities Act* 1933, this legislation contained a prohibition on waiving rights. The Court (the

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64 op cit, at 436.
65 op cit, at 438.
66 ibid.
67 op cit, at 439.
68 ibid, as a footnote.

majority opinion was delivered by Stewart J) noted that, in *Wilko v Swan*, the plaintiff was exercising a "special right", which had no equivalent in the *Securities Exchange Act*. Further, there was an extra dimension to the dispute before the Court. It involved "a truly international agreement" and "significantly different" policy considerations to those applying in *Wilko v Swan* were called for. [70]

The parties specifying in advance as to which forum disputes would be litigated, was:-

> ". . . an almost indispensable precondition to achievement of the orderliness and predictability essential to any international business transaction." [71]

The approach taken by the Supreme Court meant that the proponents of *Wilko v Swan* could still argue that the principles espoused in *Scherk v Alberto-Culver* applied only to international agreements.

In relation to international contracts, there came a further landmark decision in 1985, *Mitsubishi Motors Corp v Soler Chrysler-Plymouth Inc* [72], in which the Court reversed previous policy by holding that antitrust matters were arbitrable.

Previously, such matters were regarded as not arbitrable because of their great public significance. §4 of the *Clayton Act* permits the recovery of treble damages by any party suffering loss as a result of "anything forbidden in the antitrust laws".

The Supreme Court had spoken of the significance of the remedy and the behaviour it was designed to counter in *Hawaii v Standard Oil Co* [73], where Marshall J (who delivered the majority opinion) said:-

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69 op cit.
70 op cit, at 515.
71 op cit, at 516.
72 473 US 614 (1985).
73 405 US 251 (1972).

> "Every violation of the antitrust laws is a blow to the free-enterprise system envisaged by Congress . . . By offering potential litigants the prospect of a recovery in three times the amount of their damages, Congress encouraged these persons to serve as 'private attorneys general.' " [74]

In *American Safety Equipment Corp v J P Maguire & Co*, the Court of Appeals for the Second Circuit said that there was a "pervasive public interest" in the enforcement of antitrust law and that the nature of the claims:-

> " . . . make antitrust claims . . . inappropriate for arbitration." [75]

In *Mitsubishi v Soler* [76], the petitioner ("Mitsubishi"), had appointed the respondent ("Soler") as a distributor of motor vehicles. The agreement between the parties contained an arbitration clause, referring disputes to the Japan Commercial Arbitration Association. Disputes arose and Mitsubishi commenced an action in the District Court for Puerto Rico, seeking to compel arbitration. Soler counterclaimed on a number of grounds, including causes of action under the *Sherman Act*.

The District Court ordered the parties to arbitration, with the exception of some matters in the counterclaim. With the claims under the *Sherman Act*, the Court noted the authority of *American Safety Equipment*, but held nonetheless that the antitrust matters were arbitrable. The Court relied on *Scherk v Alberto-Culver*, noting, as in that case, the agreement between Mitsubishi and Soler was international in character.

The matter then went to the Court of Appeals for the First Circuit who reversed the District Court in part, by holding that the decision in *Scherk v Alberto-Culver* did not justify abandonment of the doctrine which required that all actions under the *Sherman Act* must go before a court.

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74 op cit, at 262.
75 op cit, at 828.
76 op cit.

The matter went to the Supreme Court. Soler's arguments before the Supreme Court were firstly, because the arbitration clause did not refer to the *Sherman Act*, or indeed statutes in general, Soler had not agreed to arbitrate matters involving statutory claims. The only way statutory claims may be arbitrated, Soler argued, is if express mention is made thereof in the arbitration agreement. Soler asserted further that, even if it had agreed to arbitrate antitrust claims, the courts had consistently held that such claims were non-arbitrable.

The majority opinion was delivered by Blackmun J. In rejecting Soler's first point, His Honour said that there was nothing in the Act implying a prohibition on the arbitration of statutory claims; further, in *Wilko v Swan* the Supreme Court had said that it was hoped that the Act would be useful in resolving controversies based on "statutes or on standards otherwise created". [77]

Blackmun J continued by noting that not all controversies involving statutory claims might be suitable for arbitration - however, this provided no basis to " . . . distort the process of contract interpretation . . . in order to ferret out the inappropriate." [78]

In other words, there is no warrant to read into arbitration agreements such kind of implied restrictions as Soler was arguing.

In any event, His Honour continued, an agreement to arbitrate does not involve a forgoing of rights; it means that whatever claims might arise will be dealt with in a forum other than the courts. [79]

With Soler's second submission, Blackmun J firstly stated that it was unnecessary to consider whether the *American Safety* doctrine remained appropriate for domestic arbitration. His Honour continued by saying that, despite the "fundamental

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77 op cit, at 625-626, referring to *Wilko v Swan* at 432.
78 op cit, at 627.
79 op cit, at 628.

importance to American democratic capitalism of the regime of the antitrust laws", the Court nonetheless felt some scepticism regarding the *American Safety* doctrine. [80]

His Honour noted the four major points comprising the *American Safety* doctrine - first, that private parties, by means of the treble damages provisions, played a pivotal role in aiding government enforcement; second, as the types of contract which led to antitrust disputes most probably were contracts of adhesion, it was inappropriate to have selection of the forum determined automatically by the terms of the contract. Third, antitrust issues required complex legal and economic analysis, which did not sit easily with the arbitral process, which emphasised expedition and simplicity. Finally, antitrust matters were "too important" to be left to arbitrators drawn from the business community, particularly ones from other jurisdictions, with no appreciation of American laws and values.

Blackmun J dismissed each of these submissions. [81] His Honour said that the treble damages provision did not preclude action taken outside of the court system. Whilst the provision has an important policing function, previous authority indicated that the remedy is essentially compensatory. [82] Its character is that of a remedy.

[Blackmun J did not make any direct reference to the consequences of the treble damages being anything other than compensatory. It seems, however, that had the provision been regarded as essentially punitive (ie, in the sense that its main purpose is to act as a deterrent, rather than to compensate), then perhaps a different approach might have been taken by the courts. If an action seeking treble damages was not regarded as compensatory, then the courts may have indeed been reluctant to allow what probably amounted to, or at least was analogous to, a prosecution, to be handled outside the court system.]

Next, there was nothing to justify regarding the forum selection as being invalidated, merely because an antitrust matter was involved. The party resisting arbitration could

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80 op cit, at 634.
81 op cit, at 632 *et seq.*

always attack the validity of the arbitration agreement. Third, the possibility that a dispute may involve complex issues was not the problem that it was supposed to be. Experts in the field could be chosen as arbitrators. Finally, there was nothing to suggest that arbitrators selected from the business community would not act competently and impartially.

Shortly before *Mitsubishi v Soler*, the Supreme Court had also looked at the issue of arbitrability in *Moses H Cone Memorial Hospital v Mercury Construction Corp.* [83] The Federal District Court had issued a stay of arbitration, pending resolution by the Court of issues concerning the arbitrability of the parties' dispute. The Court of Appeals, Fourth Circuit, lifted the stay. The Supreme Court affirmed the decision of the Court of Appeals. The Supreme Court said:-

> "The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favour of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay or a like defense to arbitrability." [84]

In *Deloitte Noraudit A/S v Deloitte Haskins & Sells* [85] the Court of Appeals, Second Circuit, referred to *Moses H Cone* and stated that the policy favouring arbitration "is even stronger in the context of international transactions". [86]

The Supreme Court completed its transition to a more "pro-arbitration" stance, firstly, in *Dean Witter Reynolds Inc v Byrd* [87], then in *Shearson/American Express Inc v McMahon* [88] and finally, by overturning *Wilko v Swan* in *Rodriguez De Quijas v Shearson/American Express.* [89]

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82 His Honour referred to *Brunswick Corp v Pueblo Bowl-O-Mat Inc* 429 US 477 (1977).
83 460 US 1 (1983).
84 op cit, at 24, 25.
85 9 F. 3d, 1060 (Second Circuit, 1993).
86 op cit, at 1063. The same Court applied *Deloitte Noraudit* in *Chelsea Square Textiles Inc, Lazar, Gribetz v Bombay Dyeing and Manufacturing Company Ltd* 189 F. 3d 289 (1999).
87 470 US 213 (1985).
88 482 US 220 (1987).

In *Dean Witter v Byrd*, a disgruntled investor brought an action in the Federal District Court against Dean Witter (a securities dealer), alleging breaches of the *Securities Exchange Act*, as well as breaches of state laws. Dean Witter sought to compel arbitration of the state law matters, but to stay the arbitration until the federal claims had been heard. Both the District Court and the Court of Appeals for the Ninth Circuit, refused the application.

Marshall J, in delivering the opinion of the Court, noted differences which had arisen between some of the Federal Courts of Appeals over the proper course of action where there was a matter involving both federal securities claims and state law claims. Some Federal Courts of Appeals had adopted what was called the doctrine of "intertwining", which meant that where arbitrable and non-arbitrable claims arose out of the same transaction and were "sufficiently intertwined factually and legally", the court may decline to make an order sending the parties to arbitration and instead, try all the matters. [90] The stated justification for this, Marshall J continued, was twofold - firstly, the courts desired to maintain their jurisdiction over federal claims (any findings by an arbitrator before the federal matters were heard might bind the courts) and secondly, hearing all the matters in the courts promoted efficiency. Other Courts of Appeals, however, took the view that the Act promoted the "strong federal policy" of requiring parties to honour agreements to arbitrate. [91] Accordingly, where parties had agreed to arbitrate, questions of efficiency were irrelevant and the agreement would be upheld.

Marshall J confirmed that the Supreme Court approved of the latter approach. His Honour said:-

> "We . . . reject the suggestion that the overriding goal of the Arbitration Act was to promote the expeditious resolution of claims. The Act, after all, does not mandate the arbitration of all claims, but merely the enforcement . . . of privately negotiated arbitration agreements." [92]

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89 490 US 477 (1989).
90 *Dean Witter v Byrd*, op cit, at 216.
91 op cit, at 217.
92 op cit, at 219.

Marshall J also noted that Dean Witter had not, in the District Court, sought to compel arbitration of the *Securities Act* claims. Accordingly, the question as to whether *Wilko v Swan* applied to claims under s10(b) and Rule 10b-5, did not arise, although His Honour noted that "numerous" lower courts had held that *Wilko v Swan* did apply to such claims.

The significance of this case, it is suggested, is in the Court holding that the honouring of agreements to arbitrate overrode arguments over "economy and efficiency".

In *Shearson v McMahon*, the Supreme Court [93] referred to the decision in *Wilko v Swan*, noting that it was "expressly based" on the belief that a judicial forum was necessary to protect the rights created under the *Securities Act*. This meant that *Wilko v Swan* could only be understood as holding that:-

> " . . the plaintiff's waiver of the 'right to select the judicial forum' . . . was unenforceable only because arbitration was judged inadequate to enforce the statutory rights created by s12(2)." [94]

O'Connor J then referred to *Scherk v Alberto Culver*, which must, Her Honour said, support the proposition that *Wilko v Swan* must be seen as:-

> " . . barring waiver of a judicial forum only where arbitration is inadequate to protect the substantive rights at issue. " [95]

Her Honour continued that *Scherk* also confirmed that where arbitration did provide an adequate remedy, then waiver of the right to select a judicial forum was

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93 O'Connor J delivered the majority opinion.
94 op cit, at 228-229.
95 ibid.

permissible. [96] O'Connor J said that the reasons for the majority decision in *Wilko v Swan*:-

> " . . . reflect a general suspicion of the desirability of arbitration and the competence of arbitral tribunals - most apply with no greater force to the arbitration of securities disputes than to the arbitration of legal disputes generally. It is difficult to reconcile Wilko's mistrust of the arbitral process with this Court's subsequent decisions . . . Indeed, most of the reasons given in Wilko have been rejected subsequently by the Court . . ." [97]

Finally, as noted above, the Supreme Court in *De Quijas v Shearson* overturned *Wilko v Swan*. This case also involved the *Securities Act* 1933. Investors had signed a "standard agreement" with a brokerage firm, which included an arbitration clause. At first instance, the District Court applied *Wilko v Swan*. The Court of Appeals, however, reversed the decision, stating that the Supreme Court had reduced *Wilko v Swan* to "obsolescence". Kennedy J delivered the opinion of the majority in the Supreme Court, noting that the traditional judicial hostility to arbitration had been eroded, both by lower courts and the Supreme Court itself. His Honour noted the dissenting judgment of Frankfurter J in *Wilko v Swan* and said that what was true in that case, was also true in *Rodriguez de Quijas* - ie, that there was nothing before the Court, nor anything of which judicial notice could be taken, to indicate that "the arbitral system would not afford the plaintiff the rights to which he is entitled". [98]

The trend has also been toward a more liberal approach in relation to the other context of arbitrability – whether an arbitration clause extends to the subject matter of a particular dispute.

In *SA Mineracao da Trinidade-Samitri v Utah International Inc* [99], the Court of Appeals (Second Circuit) said that the federal policy favouring arbitration:-

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96 ibid.
97 op cit, at 231-232.
98 op cit, at 234.
99 745 F.2d 190 (Second Circuit, 1984).

" . . . requires us to construe arbitration clauses as broadly as possible. Doubts as to arbitrability should be resolved in favour of coverage . . ." [100]

More recently, the United States Supreme Court ordered arbitration where the arbitration agreement prohibited awards of punitive damages and the respondents had alleged breaches of the *Racketeer Influenced and Corrupt Organisations* Act ("RICO"). This legislation permits treble damages to be awarded. The Court said that the "RICO treble damages provisions" were usually regarded as remedial, not punitive. Further, as the Court could not speculate as to how an arbitrator might construe the remedial provisions, arbitration should proceed. [101]

(b) the "pro-enforcement bias" of the New York Convention

Shortly after the United States had adopted the New York Convention [102], American courts began to enforce what they described as the "pro-enforcement bias" of the Convention. In *Parsons & Whittemore Overseas Co Inc v Societe General de L'Industrie du Papier* [103], the US based appellant ("Parsons & Whittemore") was unsuccessful in restraining an Egyptian corporation ("RAKTA") from enforcing an award arising out of an arbitration which had taken place under ICC rules.

Parsons & Whittemore had contracted with RAKTA to construct a paperboard mill in Alexandria. The project was to be financed by an agency of the United States State Department. In May 1967, when the project was nearing completion, Israel and the Arab States were on the verge of the Six Day War. The Egyptian government broke diplomatic ties with the United States and ordered the expulsion of all Americans, except for those who qualified for special visas. The United States retaliation included having the State Department Agency withdraw its financial support for the RAKTA project. Parsons & Whittemore abandoned the project and withdrew its personnel from Egypt. When RAKTA sought damages for breach of contract, Parsons & Whittemore relied on a *force majeure* clause in the contract, claiming that

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100 op cit, at 194.

101 *Pacificare Health Systems Inc v Book*, Supreme Court of the United States, Number 02-215, 7 April 2003.

102 The United States adopted the Convention in 1970.

performance of its obligations had been rendered impossible, because of the political situation between the United States and Egypt.

The dispute went to an arbitral panel, who ruled that reliance could have been placed on the *force majeure* clause for a limited period only. The panel also held that Parsons & Whittemore had made no more than a perfunctory attempt to secure the special visas for its personnel and that the withdrawal of financial support was insufficient justification for abandoning the project. [104]

The matter went to the Court of Appeals, Second Circuit. Smith J delivered the judgment of the Court. His Honour stated firstly that the New York Convention, as opposed to the Geneva Convention, "clearly shifted" the burden of proof to the defendant. His Honour continued that when the "history of the Convention as a whole" was looked at, there was:-

> " . . a general pro-enforcement bias informing the Convention and explaining its supercession of the Geneva Convention." [105]

Parsons & Whittemore's argument was that the award should not be enforced on the basis of public policy, as the actions of the United States Government required it, as "a loyal American citizen", to quit the project. [106] In response, Smith J stated that the Convention's pro-enforcement bias "points toward" a narrow reading of the public policy defence. His Honour said:-

> "An expansive construction would vitiate the Convention's basic effort to remove pre-existing obstacles to enforcement . . . Enforcement of foreign arbitral awards may be denied only where enforcement would violate the forum state's most basic notions of morality and justice." [107]

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103 op cit.
104 op cit, at 972.
105 op cit, at 973.
106 op cit, at 974.
107 op cit, at 973 and 974.

There was also a more pragmatic element to consider. Reciprocity was a significant issue and United States courts, in considering this defence, should proceed cautiously, otherwise foreign courts might become tempted to also apply it frequently, in response to applications to enforce awards made in the United States. [108]

In this context, Smith J continued, public policy was not to be confused with "national" policy:-

> "To read the public policy defence as a parochial device protective of national political interests would seriously undermine the Convention's utility." [109]

Intellectual property

A particular area of law where issues have arisen in relation to arbitrability is intellectual property. There is generally no concern with, eg, licensing disputes, where two private parties are concerned with allegations of contractual breach. Where, however, State-granted rights (eg, the validity of a patent) are in question, different issues arise. It would ordinarily not be expected that a private tribunal could disturb such rights. Grantham points out, however, that some jurisdictions permit questions concerning validity to be arbitrated. [110] Arbitrators in such cases act as agents of the authorities - awards are lodged in the relevant registries.

Such provisions exist in the United States [111] and Switzerland. [112]

Australia

(a) common law

At common law, Australian courts took the view that parties, once having agreed to arbitrate, should, in the ordinary course, be kept to their bargain. [113]

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108 ibid.
109 ibid.
110 Grantham, op cit, at 182-185.
111 See 35 USC § 294

Whether or not a stay was granted where one party to an arbitration agreement requested a referral to arbitration was a matter of discretion. The court's discretion was usually exercised in favour of upholding the agreement:-

> "Although the court has a discretion . . . it is a discretion to be exercised with this consideration to the forefront. Parties to international trading agreements should be able to be confident that, if they deliberately and advisedly stipulate for arbitration . . . this stipulation will be respected." [114]

(b) Section 7 of the *International Arbitration Act* 1974 (Cwth) - Constitutional validity

S7 [115] was the subject of a constitutional challenge in *Hi-Fert Pty Limited and anor v Kiukiang Maritime Carriers Inc and anor.* [116] The applicants commenced an action in the Federal Court over a contract made pursuant to a charter. (The first applicant was the consignee of a shipment of wheat; the second applicant, the consignor. The first respondent was the owner of the vessel; the second respondent, the charterer). The cargo of wheat had become contaminated during a voyage entered into under what was later described in the Full Court of the Federal Court as the "addendum contract". The applicants alleged negligence, breach of contract, misrepresentation, breach of collateral warranty and misleading and deceptive conduct under the *Trade Practices Act* 1974 (Cwth). The first respondent challenged the proceedings on the basis of an arbitration clause under which the parties agreed to arbitrate "any dispute arising from this Charter or any Bill of Lading issued hereunder" in London, under English law. The first respondent sought a stay and referral to arbitration under s7. The second respondent also sought a stay, on the basis that it would be "oppressive

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112 *Loi federale sur le droit international privé*, Article 193.1.

113 see, eg, *Huddart Parker Limited v The Ship Mill Hill* (1950) 81 CLR 502, at 508-509, per Dixon J (as he then was).

114 *Joy Manufacturing Co v A E Goodwin Limited* (1970) 91 WN 671, at 674, per Street J (as he then was).

115 The provisions of s7 of the *International Arbitration Act* 1974 are described in some detail in Chapter II.

116 (1997) 145 ALR 500.

and vexatious" if the first applicant pursued the claim against it in Australia, if an arbitration was to take place in London.

In response, the applicants challenged the validity of s7, on a number of grounds. Firstly, that, in providing for a mandatory stay, it ousted the jurisdiction of the Court and was consequently against public policy.

Tamberlin J rejected his. His Honour stated that, in considering an application under s7, the Court was in fact exercising judicial power. On this basis, s7 did not oust jurisdiction Further, His honour said:-

> " . . . determination by arbitration can hardly be said to be contrary to public policy. A statutory provision such as s7 . . . is of itself the clearest and more precise manifestation of the relevant public policy as to the way in which such disputes must be resolved." [117]

The plaintiff also argued that s7 purported to direct the Federal Court as to the conclusion it must reach in exercising its jurisdiction, where justiciable issues were before it for consideration. The applicants compared s7 with the legislation which was considered by the High Court of Australia in *Kable v Director of Public Prosecutions* [118]. The New South Wales Government had enacted legislation [the *Community Protection Act* 1994 (NSW)] which provided for the continued incarceration of a particular prisoner. Under the legislation, the prisoner (Kable) could have become liable to remain in "preventive detention" despite having served out the sentence imposed at his trial. The Director of Public Prosecutions was entitled to make application for such detention against Kable (and only against Kable – not in respect of any other prisoner). The Supreme Court of New South Wales was empowered to make the order, if it was satisfied that Kable was more likely than not to commit a serious act of violence and that it was appropriate for protective purposes that Kable remain in custody.

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117 at 505.

118 (1997) 189 CLR 51.

The legislation was struck down by the High Court as being incompatible with the exercise of the judicial power of the Commonwealth (under Chapter III of the Constitution). It required the Supreme Court of New South Wales (which, although a State Court, had been vested with federal jurisdiction) to carry out what was essentially an executive function.

Tamberlin J also rejected this argument. His Honour said that the legislation considered in *Kable* was of a different character to s7. The consideration by a court of an application under s7 involved the exercise of judicial power. There was no usurpation of judicial power. As had been held in *Scott v Avery* [119], the parties should be held to their agreement to arbitrate. [120]

The applicants then argued that if the *Trade Practices Act* 1974 (Cwth) claims were referred to arbitrators in London, this would have the effect of conferring on the arbitrators the judicial power of the Commonwealth, without regard to their qualifications, experience or expertise in relation to such claims. His Honour also rejected that submission. [121]

On appeal to the Full Court, the applicants pursued these submissions. Emmett J (with whom Branson J agreed) noted that the *International Arbitration Act* 1974 (Cwth), if valid, was based on the foreign affairs power of the Constitution. [122] All that s7 was concerned with was laying down a "general rule" under which:-

> " . . . a party to an arbitration agreement is entitled to have that arbitration agreement given effect to by the relevant court." [123]

Further, s7 did not purport to direct the manner and outcome of the exercise by the Court of its jurisdiction. [124]

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119 op cit.
120 *Hi-Fert*, op it, at 507.
121 at 509.
122 Section 51(xxix).
123 *Hi-Fert Pty Limited v Kiukiang Maritime Carriers Inc*, (1998) 159 ALR 142, at 153.
124 at 154.

(c) can parties contract out of s7?

In a decision of the Supreme Court of Victoria, *Abigroup Contractors Pty Limited v Transfield Pty Limited and Obayashi Corporation & ors* [125], Gillard J held that parties could contract out of the provisions of s7 of the *International Arbitration Act*. His Honour said that, subject to:-

> ". . . public policy and statute law, parties to a contract can agree to do anything." [126]

His Honour then noted that s7 did not contain any express provision "precluding a party . . . agreeing not to apply for a stay", and then continued:-

> "There is no suggestion that it would be contrary to public policy or that the general law precludes a party to such an agreement (*ie, an arbitration agreement*) from covenanting not to make application pursuant to s7 of the Act to stay court proceedings." [127]

His Honour did not refer to cases such as *Huddart Parker v Mill Hill* and *Joy Manufacturing v Goodwin*. Whilst both of these cases were decided under the common law, both the High Court and New South Wales Supreme Court referred to the desirability of holding parties to their bargain. If an agreement is made to arbitrate, it seems odd to allow the parties, at the same time, to waive their rights should one of them commence court proceedings.

It is suggested that public policy might dictate that it is against public policy to waive rights under s7, if there is an arbitration agreement.

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125 unreported, Supreme Court of Victoria. Austlii reference - [1998] VSC 103 (16 October 1998).

126 op cit, paragraph 86, Austlii report.

127 op cit, paragraph 98.

(d) the issue of arbitrability in Australia

There have been a number of decisions in relation to s7 of the *International Arbitration Act*, over whether Trade Practices claims may be the subject of reference to arbitration - ie, whether such claims were arbitrable. In the New South Wales Supreme Court decision of *Flakt (Australia) Limited v Wilkins and Davies Construction Co Limited* [128], McLelland J considered the provisions of sub-section 7(2) and, in particular, the word "matter". His Honour said that "matter":-

> " . . . denotes any claim for relief of a kind proper for determination in a court. It does not include every issue which would or might, arise for decision in the course of the determination of such a claim." [129]

These observations were quoted with approval by Beaumont J in *Allergan Pharmaceuticals Inc and anor v Bausch and Lamb Inc and anor* [130]. The applicants had commenced proceedings in the Federal Court, alleging breach of contract, infringements of patents and misleading or deceptive conduct under s52 of the *Trade Practices Act*. The respondents sought a stay, on the basis of an arbitration clause under which the parties agreed to arbitrate in New York "any controversy or claims arising out of or related to this Agreement." Beaumont J referred to *Flakt* and continued to the effect that the pleadings should be referred to, to see if any breach of the Agreement was alleged. If so, all such claims should be stayed. [131] In respect of the Trade Practices claims, however, no such order could be made, as they did not arise out of, or relate to the relevant agreement. His Honour said:-

> ". . . the statutory causes of action now sued upon exist independently of contract . . . Conduct of the kind proscribed by Part V of the *Trade Practices Act* will be established, if at all, irrespective of the contractual relations of the immediate parties . . .

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128 (1979) 2 NSWLR 243.
129 op cit, at 250.
130 (1985) ATPR 40-636.
131 op cit, at 47,173.

> The same observations can be made of the claimed infringement of the letters patent. Again, the cause of action is statutory only . . ." [132]

As the Trade Practices claims were independent of the agreement, they were not contemplated by the arbitration clause. If the *Trade Practices Act* permitted remedies in the circumstances, then this was coincidental. Even if the expression "relating to" was given a wide meaning, the Trade Practices claims did not relate to the agreement.

A different view was taken by the New South Wales Court of Appeal in *IBM Australia Limited v National Distribution Services Limited.* [133] The Court considered an arbitration agreement which provided for a submission in the case of "any controversy or claim arising out of or related to this agreement or the breach thereof". The Court held that Trade Practices claims could be referred to arbitration. Clarke JA said that the arbitration clause should not be construed narrowly, nor should its terms be read down. [134] The consequences of adopting a narrow construction, His Honour continued, would be that the Trade Practices claims would be determined by the court, whilst the contractual claims would have to go to arbitration. This would follow even where the same representations were said to found causes of action both under Trade Practices and the contract. [135] Clarke JA then said:-

> "The parties could hardly be thought to have contemplated that the arbitration clause would work that way. It is far more likely that they intended that all disputes between them concerning the terms of the contract, the performance of it and matters connected, in a real sense, with the contract should be referred to the one tribunal for determination." [136]

Further, if Trade Practices claims could not be referred to arbitration, the splitting of actions would be inefficient and costly. [137]

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132 op cit, at 47,173-174.
133 [1991] 22 NSWLR 466.
134 op cit, at 483.
135 ibid.
136 ibid.
137 ibid.

Kirby P (as he then was) agreed that the Trade Practices claims could go to arbitration. His Honour's emphasis was somewhat different to that of Clarke JA. Kirby P thought that the circumstances were governed by *Government Insurance Office of New South Wales v Atkinson-Leighton Joint Venture* [138], where the High Court looked at the issue of whether an arbitrator had the power to award interest on the amount of an award. Mason J (as he then was) said in that case that the real question was whether there was, in the submission to arbitration, an implied term that the arbitrator was empowered to award such relief as could a court dealing with the same subject matter. [139] Mason J then noted that, as under s94 of the *Supreme Court Act* (NSW), the Court was entitled to award interest from the time the cause of action arose to date of judgment, it followed that it was implied in the submission, there was authority for the arbitrator to award interest. The Court had a supervisory function over arbitration and further, an award could be enforced as if it were a judgement or order of the Court. [140] Murphy and Wilson JJ agreed with Mason J.

Applying this, Kirby P held that the arbitrators had power to consider the claim. His Honour said that the effect of the decision in *Government Insurance Office of NSW v Atkinson Leighton Joint Venture* was that:-

> " . . . the very purpose of a reference to arbitration will frequently be to confer on the arbitrator the powers which would be enjoyed, even by statute only, by the court of law of competent jurisdiction that would otherwise hear the case . . . " [141]

Whilst it may only be a question of emphasis, with respect to Kirby P, it is submitted that the approach of Clarke JA is to be preferred. In *Government Insurance Office (NSW) v Atkinson-Leighton*, Mason J said that the arbitrator was to have the same powers as the court. What must be looked at is the nature of the matter at issue; if the matter involves eg, a damages claim, then the plaintiff/claimant must be entitled to all remedies available. The claimant should be entitled to receive from an arbitrator

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138 (1981) 146 CLR 206.
139 op cit, at 247.
140 ibid.
141 *IBM v National Distribution Services*, op cit, at 480.

that which the claimant would receive from a court. This is somewhat different, it is suggested, to the question as to the jurisdiction of the arbitrator.

As Clarke JA said, however, to have only contractual matters referred to an arbitrator whilst the question of statutory breaches remained with the court, would not, in the vast majority of cases, accord with reality. If the parties to a commercial contract decide upon arbitration as their preferred method of dispute resolution, they would be (as Clarke JA noted) extremely unlikely to *impliedly* reserve some causes of action for the courts alone.

In *Paper Products Pty Limited v Tomlinsons (Rochdale) Limited* [142], French J (in the Federal Court) said that where the arbitration clause was "sufficiently elastic", a more liberal approach would be warranted. A broad interpretation was justified on the grounds that the parties would be unlikely to have intended that their disputes would be divided into matters, some of which could be arbitrated, but others must be heard by a court. Where the parties had, however, agreed upon a restricted form of words, then this would be given effect to. [143]

The New South Wales Court of Appeal in *Francis Travel Marketing Pty Limited v Virgin Atlantic Airways Limited* [144], applied *GIO (NSW) v Atkinson-Leighton* and held that an arbitration clause which provided for disputes "arising out of" the agreement covered Trade Practices claims, which could be referred to arbitration. [145] The Court noted with approval the decision in *Mitsubishi v Soler.* [146]

It should be noted that *Francis Travel* was distinguished in the Federal Court decision in *Hi-Fert Pty Limited v Kiukiang Maritime Carriers Inc.* [147] In the Full Court, Emmett J (with whom Branson J agreed) firstly stated that reliance on the authority of *Government Insurance Office (NSW) v Atkinson-Leighton* was "unsound" in the context of whether Trade Practices claims might be arbitrated. His Honour said:-

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142 (1993) 116 ALR 163.
143 at 172.
144 (1996) 39 NSWLR 160.
145 at 165.
146 at 167.

> ". . . the right to interest on damages is not an independent cause of action. It is simply a mechanism to ensure that a claimant is not prejudiced by inevitable delay . . . That is not a justification for a conclusion that a completely independent cause of action is to be implied as having been referred to arbitration simply because it deals with a similar subject matter as those questions which are expressly referred to arbitration." [148]

His Honour noted the decision in *Francis Travel* and said that where a claim arose in respect of conduct antecedent to the making of the contract, the dispute did not arise "*from* the contract." [149] (original emphasis).

The circumstances in *Francis Travel* could be distinguished. There, the relevant agreement was an "integral part" of the course of action. [150] In the *Hi-Fert* case:-

> "There was no juridical connection between the conduct and the charter contract as there was between the agency agreement and the relevant conduct in *Francis Travel*. The question there was whether the agency agreement had come to an end because of the conduct. Here . . . the charter contract was no more than the background against which the conduct occurred.
>
> The parties have chosen restricted language to describe those disputes which are to be settled by arbitration. The alleged representations . . . had nothing to do with the performance of the charter contract." [151]

Emmett J held that none of the Trade Practices claims arose from the charter contract. His Honour continued that it was, therefore, not necessary to consider whether, in general, such claims were capable of being settled by arbitration within the meaning of s7(2) the *International Arbitration Act*. As His Honour noted, however, substantial argument had been directed towards that question and it was appropriate to make some observations.

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147 (1998) 159 ALR op cit.
148 op cit, at 159.
149 op cit, at 161.
150 op cit, at 162.
151 ibid.

His Honour stated that whilst the *Trade Practices Act* did not confer jurisdiction on arbitrators in London, it was nonetheless possible for parties to refer a Trade Practices claim to arbitrators. [152] There was one proviso – a party could not be compelled to arbitrate if the effect was to exclude the operation of the *Trade Practices Act*. [153]

Emmett J also noted that another potential difficulty presented itself, as the Trade Practices claims did not fall under the arbitration clause. While a stay under s7(2) of the Act could be ordered in respect of the arbitrable claims (so that arbitration could proceed in London), the Trade Practices claims would have to be heard in the Federal Court. This was the result of the operation of s11 of the *Carriage of Goods by Sea Act* and s7 of the Act. [154]

In *ACD Tridon Inc v Tridon Australia Pty Ltd and ors* [155], a decision of the New South Wales Supreme Court, the plaintiff applied to the Court seeking a number of orders, including the invalidation of share transfers, rectification of the share registry and that the first defendant be wound up. The parties were subject to various agreements which contained arbitration clauses. Austin J considered that certain disputes could be referred to arbitration, but that the application for winding up and the rectification issue could not. His Honour stated that public policy considerations "operate against" referring to arbitration such matters, as they affected not merely the parties to the dispute, but third parties. [156]

A compromise was reached when the parties agreed to the Court ordering that all matters be referred under the Supreme Court Rules to a referee, who would report to the Court and make certain recommendations. [157]

Austin J also noted that whilst Australian courts had not adopted the public policy approach of a liberal construction of arbitration clauses, nonetheless:-

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152 op cit, at 163.
153 ibid.
154 op cit, at 167, et seq.
155 [2002] NSWSC 896.
156 at paragraph 191, 192.
157 at paragraph 246.

" . . . reflection on the likely intention of the parties will steer them away from any narrow construction." [158]

"Developing" nations and arbitrability

(a) issues

As noted, it is now public policy in many jurisdictions to promote commercial arbitration. Matters previously deemed unsuitable for arbitration (such as the enforcement of anti-trust legislation), may now be referred. The marked shift in public policy in Western countries towards favouring commercial arbitration, however, may not suit the priorities of developing States.

Developing countries may take the view that public interest dictates that certain matters ought to remain within the public sphere. For some States, accordingly, the national interest requires that constraints be placed on the concept of arbitrability.

In this vein, Sornarajah criticises the UNCITRAL Model Law for designating practically all activity to the level of mere commercial activity, with all disputes capable of resolution by private means.

In particular, the author refers to exploitation agreements and concessions:-

" . . . countries may not lightly accept the notion in the Model Law that these agreements could be removed from the public law sphere by a mere commercial contract." [159]

States which depend on relatively few sources of income from eg, the exploitation of natural resources (which is usually carried out by transnational corporations, the activities of which can be difficult for individual States to control) can, perhaps not surprisingly, take the view that to cede control over their industries and economic

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158 at paragraph 120.

159 op cit, at 16.

policy (by allowing cases involving significant development projects or trade issues to go to arbitration) would be anathema.

Weisbrot notes that Developing States also face a change in economic theory, emanating from liberal economic theory. Previously, "development economics" recognised that Developing States needed greater protection and more State intervention than did advanced economies.

That has changed, with the advent of what has been described as "monoeconomics" which is:-

> " . . . the belief that there are universal laws of economics that apply to all economies." [160]

Weisbrot continues that monoeconomics:-

> " . . . translates into following the dictates of the global economy." [161]

The programs of the IMF and the World Bank are "manifestations of the adoption of monoeconomics." [162] The imposing of universal prescriptions on all economies by these international institutions, however, leads to economic imbalances only being maintained.

These organs:-

> " . . . reinforce and exacerbate the existing distribution of wealth and power, as well as the division of labour between rich and poor nations." [163]

Kirry's arguments could be adapted to these considerations. The author states that arbitrability must be considered in light of international public policy. An

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160 Weisbrot, "Globalization for Whom?", (1998) 31 *Cornell International Law Journal*, Symposium Issue, Number 3, 631, at 634.

161 ibid.

162 ibid.

163 Weisbrot, op cit, at 654.

international public policy which recognised the special needs of developing countries could recognise that certain disputes should be litigated *via* public, rather than private, processes.

(b) examples of disputes –

(i) CalEnergy v PLN

In a recent article, Kantor highlights difficulties which arose out of arbitrations in Indonesia and Pakistan. [164]

In 1994, CalEnergy Company Inc ("CalEnergy") [165] formed two special purpose subsidiary companies ("Himpurna" and "Patuha") to enter into agreements with Perusahaan Listruik Negara ("PLN"), an Indonesian State-owned enterprise. The agreements were for the supply of power from two geothermal fields in Java. PLN was to purchase power generated by Himpurna and Patuha [under a United States Dollar ("USD") denominated tariff] for 30 years. Another Indonesian instrumentality, Pertamina, entered into contracts with the two developers in relation to the operation of the geothermal fields. The Indonesian Ministry of Finance issued letters of comfort to Himpurna and Patuha, by which the Indonesian Government undertook to cause PLN and Pertamina to honour and perform their obligations under the relevant agreements.

As has been well documented, Indonesia (along with other countries) suffered from the onset of the "Asian crisis" in 1997. What followed was considerable internal disruption, both economic and social. The value of the rupiah declined dramatically, which greatly stretched PLN's ability to purchase power under the USD-denominated tariff. PLN ultimately refused to accept power.

Himpurna and Patuha commenced arbitration proceedings against PLN. It was argued by PLN before the arbitrators that CalEnergy "may have used links" with the then Indonesian leader, President Suharto, to win contracts in Indonesia. The

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164 Kantor, "International Project Finance with Public Sector Entities: When is Arbitrability a Fiction?" 24 *Fordham International Law Journal*, 1122, et seq. (2001). Most of the factual background referred to in relation to these disputes is taken from Kantor's article.

165 CalEnergy Company Inc is now known as MidAmerican Energy Holdings Company.

arbitrators found for them against PLN, awarding some USD 390m damages to Himpurna, and USD 180m to Patuha. [166]

Himpurna and Patuha then commenced arbitral proceedings against the Indonesian Government, under the letters of comfort. Before the proceedings had progressed very far, Pertamina (who was not a party to the arbitrations) and PLN brought actions in the Central Jakarta District Court. The Court issued an injunction preventing enforcement of the awards as well as the arbitral proceedings against the Government.

Nonetheless, the arbitral tribunal decided to convene in the Hague. The Indonesian Government approached the District Court of the Hague, seeking an injunction to prevent the arbitration proceeding. The Court rejected the application. [167] The arbitration was set to commence on 22 September 1999. A rather extraordinary event then occurred. The Indonesian Government did not appear before the Arbitral Tribunal. The President of the Arbitral Tribunal (Jan Paulsson) announced that the Indonesian arbitrator (appointed by PLN), Professor Priyatna, a former deputy Attorney-General of Indonesia had seemingly disappeared. It transpired that Professor Priyatna had in fact arrived in the Hague, but had been forcibly removed back to Indonesia. [168]

The removal of the arbitrator was a blatant and inexcusable interference with the arbitral process. What it was intended to achieve is not clear. It did not prevent the remaining members of the Arbitral Tribunal from discharging their duty. The Arbitral Tribunal found against the Government, in the same amount of damages as against PLN. [169]

Himpurna and Patuha then claimed under their political risk insurance, and the insurers, claiming rights of subrogation, demanded payment of the amounts awarded from the Government, which it refused to do.

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166 *Himpurna California Energy Ltd v PT (Persero Perusahaan Listruik Negara*, Yearbook Commercial Arbitration XXV (2000), 13, at 107.

167 *Himpurna v PT Persero*, op cit, at 153, 154.

168 op cit, at 155,156.

169 Op cit, at 214, 215.

Kantor notes that, at the time, there was considerable public feeling in Indonesia that many agreements of the Suharto Government were corruptly entered into, and that, in particular, the energy agreements were substantially overpriced as a result of such corrupt behaviour. [170] The involvement of the Suharto family in many enterprises has been noted, but they seemed to have had a particular interest in energy projects. The Suharto family and their cohorts had become involved in a large number of power purchase agreements ("PPAs"):-

> " . . . all the [*Suharto*] kids and cronies elbowed in and demanded their own PPAs." [171]

[It should be noted that the Arbitral Tribunal held that there was no evidence of corruption as alleged by PLN. [172] The Tribunal also held that PLN had failed to establish that, on the basis of the catastrophic fall in value of the rupiah, it should be entitled to succeed on a plea of *rebus sic stantibus*. Economic crises are not unknown events – PLN had failed to look after its own interests, in relation to events which must have been (or should have been) within their contemplation at the time of entering the agreements.] [173]

(ii) HubCo v WAPDA

The disputes in Pakistan also involved energy contracts and arose in the context of significant internal political upheaval. In 1992, the Hub Power Company Ltd ("HubCo" - a public company with United States as well as Pakistani shareholders) entered into an agreement to sell power to WAPDA, a Pakistani Government instrumentality. WAPDA's obligations were guaranteed by the Pakistani Government, led at that time by Prime Minister Nawaz Sharif.

A new government led by Benazir Bhutto came to power in 1993 and negotiated amendments to the agreement. In 1996, Ms Bhutto was forced from office and, in

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170 at 1143, 1144.

171 Anonymous interviewee – Henisz and Zelner, *The Political Economy of Private Electricity Provision in Southeast Asia,* Working Paper of the Reginald H Jones Center, Wharton School, University of Pennsylvania, February, 2001.

172 op cit.

173 op cit, at 62-65.

1997, Nawaz Sharif returned as Prime Minister. Allegations were made at ministerial level in the Sharif Government that the Bhutto-era amendments had been procured by corrupt means. Notices to terminate the agreement were issued. Other disputes arose over tariff adjustments made by Pakistani courts. HubCo commenced arbitration proceedings against WAPDA. WAPDA instigated proceedings in the Lahore High Court, arguing that the Bhutto-era amendments were fraudulent agreements, procured by corrupt means. The Lahore High Court issued an anti-arbitration injunction. [174]

After a "plethora of proceedings", the parties came before the Pakistan Supreme Court. [175] The Supreme Court upheld the anti-arbitration injunction. [176] The majority noted that there was *prima facie* evidence of corruption in relation to the Bhutto-era amendments. Consequently, the matter could not go to arbitration. Only the Pakistani courts could hear allegations of corruption. [177]

Comments

The move towards a more liberal view of arbitrability in some (mostly Western) jurisdictions has been notable. Such jurisdictions readily enforce agreements to arbitrate and there is very little (by way of subject matter) that is considered as not being arbitrable.

This obviously creates potential for conflict with "developing" States. It is suggested that public policy ought to recognise that developing States will take a different view from Western States on the question of arbitrability. It is recognised that it will be difficult in many cases to determine whether some "local" intervention is justified, as there will often be a myriad of issues clouding the situation when political and financial interests clash.

Kantor states that the courts interfering in both the Indonesian and Pakistani disputes was unwarranted. This may be correct from a legal viewpoint. It is perhaps

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174 Noted by Kantor, op cit, at 1154.

175 Barrington, "Hubco v WAPDA: Pakistan Top Court Rejects Modern Arbitration", 11 *American Review of International Arbitration* (2000), 385, at 386.

176 Barrington notes that the proceedings in the Pakistan Supreme Court were Civil Appeals 1398/99 and 1399/99, dated 14 June 2000 – Barrington, op cit, at 385.

177 Barrington, op cit, at 390.

explicable, however, why the courts in both Indonesia and Pakistan may have felt that control over the disputes should have remained in "local" hands. In both cases, outgoing officials responsible for the relevant agreements had been discredited and accused of large scale corruption. Both countries were experiencing significant economic and social problems.

Of course, allegations of corruption can be convenient for political purposes. Whilst it has been widely reported that both the Indonesia and Pakistani Governments were significantly corrupt, Kantor notes that (in relation to the Indonesian matters, at least) no specific allegations were proved in relation to the contracts in question. [178] Nonetheless, the local courts went to some lengths to keep the matters in "local" hands, not wishing to see a foreign arbitral tribunal decide the issues.

As noted, this might be explained in part by the different internal conditions (then prevailing) of the countries involved as much as allegations of corruption. Further, very large sums were involved - obligations were usually denominated in USD. As an example, the awards in the Himpurna and Patuha arbitrations totalled some USD 570m.

None of this, of course, excuses the removal of Professor Priyatna by the Indonesian Government. Once Indonesia had nominated its arbitrator and the Arbitral Tribunal convened, the arbitral process should have been respected.

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[178] See above in this Chapter.

CHAPTER VI

PUBLIC POLICY AND THE ENFORCEMENT OF AWARDS

" . . . *the public policy exception is very narrow.*" [1]

Changes in policy

It was seen in Chapter V that courts and legislatures in the jurisdictions noted have become more "pro-arbitration." This has involved a significant change in public policy on the part of courts. In these jurisdictions, another shift in public policy has occurred, involving the enforcement of arbitral awards. The "hands-off" approach has flowed through to enforcement.

It has become the norm that awards should be enforced with a minimal amount of interference. The tendency has been, accordingly, in recent times to read down the breadth of public policy as a defence to an application for enforcement:-

> " . . . the growing awareness of the courts for the specificity of international economic arbitration has lead to the development of a restrictive notion of ordre public international which is distinct from the notion of ordre public applied to domestic awards . . . (this) restrictive notion . . . limits interference with international arbitral awards to a minimum." [2]

A rather distinct outcome has emerged as a result of this – the public policy defence has, in essence, been rendered ineffective, by courts declaring that it is only to be invoked in (virtually) extreme circumstances.

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1 *CBS Corporation v Wak Orient Power Light and Light Ltd* 2001 US Dist LEXIS 4515 (ED Penn.)

An examination of some of the cases involving the public policy defence under Article V.2(b) of the New York Convention shows that, in general, the reasons for narrowing the application of public policy are connected with perceptions of the purposes of the Convention.

Public policy is "international"

First, as noted in Chapter IV, the public policy referred to under both the Convention and UNCITRAL Model Law, is not the "domestic" public policy of the forum state. A distinct form of public policy is applied - one that involves the "international" concerns of States.

Van den Berg states that the distinction between domestic and international public policy is marked by a narrowing of focus:-

> " . . . what is considered to pertain to public policy in domestic relations does not necessarily pertain to public policy in international matters . . . the number of matters considered to fall under public policy in international cases is smaller than that in domestic cases. " [3]

The reason for this different (and narrower) focus is stated by van den Berg as being connected with the effectiveness of the Convention. It was initially feared that if courts had broad public policy considerations to apply, then:-

> " . . . the Convention's public policy provisions could be used by the courts to take away a great deal of its effectiveness . . ." [4]

In *Renusagar Power Co Ltd v General Electric Co* [5], a different emphasis was made. In that case, the Supreme Court of India noted that the expression "public policy" as used in India's *Foreign Awards Act* (which was enacted to give force to the New York

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2 Berger, op cit, at 670.
3 Van den Berg, op cit. at 360.
4 op cit, at 366.

Convention) refers not to the public policy of India, but to the doctrine of public policy as applied in private international law. The Court said that:-

> " . . . the application of . . . public policy in the field of conflict of laws is more limited than that in the domestic law and courts are slower to invoke public policy in cases involving a foreign element than when a purely municipal legal issue is involved." [6]

The reason for the limitation, the Court stated, was explained by Graveson:-

> "This concern of law in the protection of social institutions is reflected in its rules of both municipal and conflict of laws. Although the concept of public policy is in the same nature in these two spheres of law, its application differs in degree and occasion, corresponding to the fact that transactions containing a foreign element may constitute a less serious threat to municipal institutions than would purely local transactions." [7]

Graveson's view that a foreign transaction "may" be less of a threat to local institutions, it is submitted, appears misconceived, at least in one respect. Graveson's view is qualified (ie, a foreign transaction *may* pose less of a threat), but if public institutions are requested to formally enforce a right arising or obtained in another jurisdiction, then surely considerations over preserving the integrity of municipal institutions are the same irrespective of whether the right is "foreign" or "local" in origin.

Further, to return to van den Berg's point, the narrowing of the application of public policy can present its own difficulties. If public policy is restricted (or even ignored), how is the public interest to be defended?

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5 Yearbook Commercial Arbitration XX (1995) 681.

6 at p. 697.

7 *Renusagar* case, ibid, where the Court referred to Graveson, *Conflict of Laws*, 7Th edition, 1974, at 165.

"Foreign" judgments

Second, it may also be appropriate to consider public policy within the context of developments in the enforcement of foreign judgments. In Chapter I, note was made of the early recognition of judgments obtained in other jurisdictions. Courts were, on the basis of comity, prepared to recognise and enforce such judgments, provided that they were satisfied that certain standards had been observed in the jurisdiction where the judgment had been obtained.

The *Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters* [8] ("1971 Hague Convention"), as its title suggests, provides for the recognition and enforcement of foreign judgments rendered by the courts of Contracting States. Article 5(i) of the 1971 Hague Convention provides that recognition and enforcement may be refused if recognition or enforcement:-

> " . . . is manifestly incompatible with the public policy of the State addressed."

As with the New York Convention, the tendency has been to regard the public policy defence as being of very limited application:-

> ". . . recognition or enforcement must be . . . 'manifestly' incompatible . . . (t)his indicates that the weapon of refusal must be rarely invoked and only as a last resort." [9]

It will not be enough if the foreign court has made a mistake with regard to the facts, or the law, unless "induced by fraud"; nor will misapplication of the court's own domestic law suffice.

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[8] Concluded on 1st February 1971. The Convention is in the process of being reviewed by a Special Commission of the Hague Conference on Private International Law.

[9] Preliminary Document Number 11, *Report of the Special Commission* (drawn up by Nygh and Pocar) on the *Future Hague Convention on International Jurisdiction and the Effects of Judgments in Civil and Commercial Matters,* Hague Conference on Private International Law, 1999.

In relation to public policy, the issue for the State addressed is "the recognition and enforcement that is requested." [10] One example of this can be seen in the reluctance of some States to enforce judgments which reflect punitive damages.

Should awards be treated in like fashion to judgments?

What is perhaps a more important comparison, however, is that judgments (even default judgments) are the result of what are (usually) transparent and public processes, rather than private processes. If public policy is to be applied restrictively in the enforcement of foreign judgments, such an approach might be more understandable than in the case of arbitral awards. As noted, an award follows a private hearing, not a public process.

Courts have public duties; they also function publicly . In court, a judge has wider interests and duties and so do advocates.

Arbitrators, however, whilst they have a duty to apply the law, are primarily responsible only to those who appoint them.

It must follow that arbitration hearings are not directly comparable with court proceedings. Arbitrations are not subject to the same transparent and accountable processes. Consequently, it is not appropriate to suggest that the role of public policy in the enforcement of arbitral awards should be analogous to that applied in the enforcement of judgments.

The effect of both the New York Convention and the UNCITRAL Model Law, however, is to elevate awards to a status comparable with court judgments. Awards will, unless a specified defence applies, be recognised and enforced by courts. It is therefore difficult to see why arbitral awards should not be subject to greater scrutiny than are judgments, so as to ensure that when public processes are invoked in aid of

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[10] Preliminary Document Number 9, *Synthesis of the Work of the Special Commission*, compiled by Kessedjian, *Future Hague Convention on International Jurisdiction and the Effects of Judgments in Civil and Commercial Matters*, Hague Conference on Private International Law, 1998.

the enforcement of awards, the integrity of such processes remains, so far as is possible, intact.

Considerations of the "comity of nations" - not relevant to commercial arbitration

In the context of the enforcement of judgments and considerations of comity, a recent decision in the High Court of Singapore might be noted. In *Re An Arbitration Between Hainan Machinery Import and Export Corporation v Donald & McArthy Pte Ltd* [11] concerned an application to refuse recognition and enforcement of an award on various grounds, including that enforcement would violate the public policy of Singapore, as the award did not decide on the real issues in dispute. Prakash J found that the public policy defence was not made out - there was no allegation of fraud or illegality and accordingly, "enforcement would not be injurious to the public good." [12] Prakash J continued:-

> "As the plaintiffs submitted, the principle of the comity of nations requires that the awards of foreign arbitral tribunals be given due deference and be enforced unless exceptional circumstances exist." [13]

It was noted in Chapter I that the Supreme Court of the United States referred to the comity of nations in *Hilton v Guyot* [14] - the recognition that nations afford to the legislative, executive and judicial acts of other nations. Comity consequently has a public character - the recognition by the public institutions of one State for the like institutions and acts of other States.

It overextends the concept of the comity of nations for courts to recognise the acts and orders of private tribunals in the same way that the acts and orders of public institutions are recognised. Of course, distinguished arbitrators bring great abilities, experience and integrity to the resolution of disputes. Whilst the recognition of and deference to the abilities of particular arbitrators can most certainly be appropriate,

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11 1996 - 1 SLR 34; 1995 SLR Lexis 564.
12 op cit, at 46; 35.
13 ibid.
14 op cit, at 164.

that ought not be based on considerations of the comity of nations, as this is reserved for the public arena - the recognition of the acts and processes of the public institutions of another State.

The public policy defence is construed narrowly

(a) United States

Perhaps the leading case is the Court of Appeals (Second Circuit) decision in *Parsons & Whittemore Overseas Co Inc v Societe Generale de L'Industrie du Papier (RAKTA)*, where the Court said that the Convention has a "general pro-enforcement" bias. Consequently, an expansive construction of the public policy defence would:-

> " . . . vitiate the Convention's basic effort to remove pre-existing obstacles to enforcement." [15]

Further, there were considerations of reciprocity - courts should invoke public policy "with caution", lest other States courts "frequently accept it" in relation to awards rendered in the United States. The Court held that public policy should consequently have a limited application. It should be invoked:-

> " . . . only where enforcement would violate the forum state's most basic notions of morality and justice." [16]

The Court also warned against confusing public policy with "national interest":-

> "To read the public policy defence as a parochial device protective of national political interests would seriously undermine the Convention's utility. This

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15 op cit, at 973.
16 Op cit, at 974.

provision was not meant to enshrine the vagaries of international politics under the rubric of 'public policy'". [17]

Parsons & Whittemore has been described as both a "seminal" decision [18] and a "landmark" decision. [19]

In *International Navigation Ltd v Waterside Ocean Navigation Co Inc* [20], the Court of Appeals, Second Circuit, confirmed that the public policy defence must be construed in light of the overriding purposes of the Convention. [21] The Court followed *Scherk v Alberto Culver* in holding that part of the "overriding purpose" of the Convention was to unify the standards by which awards are enforced. Applying *Parsons & Whittemore*, the public policy defence should then apply only where enforcement would violate the "most basic notions of morality and justice" of the forum State. [22]

In another example of upholding the Convention's "pro-arbitration bias", in *American Construction Machinery & Equipment Corporation Ltd v Mechanised Construction of Pakistan Ltd* [23], the District Court (SDNY) ignored the fact that a Pakistani court had declared both the arbitration agreement and the award invalid, when the parties had agreed that disputes were to be referred to the ICC. The Court stated that public policy would be violated if the award was *not* in fact confirmed. [24] Consequently, the Convention's "pro-enforcement bias" overrode considerations of comity.

In *National Oil Corp v Libyan Sun Oil Co* [25], the District Court (Delaware) reaffirmed the distinction between public policy and foreign policy. The petitioner ("NOC") was

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17 ibid.

18 Stewart, "National Enforcement of Arbitral Awards Under Treaties and Conventions", in Lillich and Brower (eds), *International Arbitration in the 21st Century: Towards 'Judicialization' and Uniformity?* Transnational Publishers, at

19 Bouzari, "The Public Policy Exception to Enforcement of International Arbitral Awards: Implications for Post-NAFTA Jurisprudence", 30 *Texas International Law Journal* (Winter 1995), 205, at 211.

20 737 F.2d 150 (Second Circuit, 1984).

21 op cit, at 152.

22 ibid.

23 659 F. Supp. 426 (SDNY, 1987).

24 op cit, at 429.

a Libyan State-owned corporation which, in November 1980, had entered into an Exploration and Production Sharing Agreement ("EPSA") with the respondent ("Sun Oil"), a Delaware corporation. Under the EPSA, Sun Oil was to "carry out and fund an oil exploration program in Libya." In December 1981, Sun Oil invoked the *force majeure* provisions of the EPSA, claiming that US State Department orders prohibiting certain dealings with (and travel to) Libya prevented it from performing its obligations. Arbitration proceeded in Paris. The Arbitral Tribunal held that the *force majeure* provisions did not apply - the State Department orders were qualified and it would have been possible for Sun Oil to have made alternative arrangements to perform the EPSA. The Tribunal found for NOC, who commenced enforcement proceedings in Delaware.

Sun Oil argued *inter alia* that that it would be against public policy to enforce the award, as to do so would penalise Sun Oil for obeying the foreign policy objectives of the United States. Confirmation would also be inconsistent with the Government's anti-terrorism policy and would result in the provision of moneys for the funding of terrorist activities. Sun Oil said that Libya's activities threatened "most standards of behaviour." [26]

The Court rejected these arguments, stating that public policy and foreign policy were "not synonymous". [27] The Court referred to the passage in *Parsons & Whittemore* which addressed that "very issue" [28], stating that the Libyan Government's behaviour was "simply *beside the point.*"[29] (original emphasis). The Court also noted that Sun Oil had "demonstrated its own brand of hypocrisy" by signing the EPSA at a time when Libya was "*already* considered to be hostile to US interests." (original emphasis). [30]

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25 733 F. Supp 800 (D. Delaware, 1990).

26 *NOC v Sun Oil*, op cit, at 819.

27 ibid.

28 *Parsons & Whittemore*, op cit, at 974 - "To read the public policy defence as a parochial device protective of national political interests would seriously undermine the Convention's utility. This provision was not meant to enshrine the vagaries of international politics under the rubric of 'public policy.' "

29 op cit, at 820.

As the Arbitral Tribunal had concluded that that there was no justification for invoking *force majeure*, the Court would not reopen that issue and, as Sun Oil's arguments on public policy failed, the award would be enforced.

In *Industrial Risk Insurers v MAN Gutehoffnungshütte GmbH* [31], the Court of Appeals, Eleventh Circuit, noted that previous decisions involving domestic arbitrations had held that the enforcement of awards should only be refused, if:-

> " . . . the award violates some "explicit" public policy, which is 'well-defined and dominant . . . [*and*] ascertained 'by reference to laws and legal precedents and not from general considerations of supposed public interests.' " [32]

The Court continued:-

> "We believe that rule applies with equal force in the context of international arbitral awards." [33]

The Court then noted that *Parsons & Whittemore* was authority for the proposition that the public policy defence should be "construed narrowly." [34]

What the Court is saying is that, when a court considers an application to enforce an arbitral award (whether domestic or international), public policy has an extremely narrow role. The only policy issues considered are "explicit" public policy issues, which are limited to well-established principles in the application of the law and which are to be distinguished from public policy "at large", which may (indeed must) take account of general interests.

More recently, in *Dandong Shuguang Axel Corporation Ltd v Brilliance Machinery et al* [35], the Court also applied *Parsons & Whittemore*, stating that the defence is "construed narrowly", as the "public policy in favour of arbitration" is strong. [36]

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30 op cit, n.33.
31 op cit.
32 op cit, at 1445.
33 ibid.
34 ibid.
35 2001 US Dist Lexis 7493 (ND California).

This is a constant theme in United States decisions - to the extent that it seems that the "pro-enforcement bias" of the New York Convention has become the prime consideration, overriding all other considerations, in actions under Article V.2(b).

(b) Switzerland

A similar approach to that of the United States Courts can be seen in some Swiss decisions. Van den Berg notes a 1975 decision of the Swiss Federal Supreme Court (involving a decision under the Geneva Convention), in which it was said that the extent of the application of Swiss public order was more restrictive in relation to foreign awards, than in the application of foreign law. For the enforcement of an award to be refused, there must be a "violation of fundamental principles of the Swiss legal order, hurting intolerably the feeling of justice . . . ". [37]

In a more recent decision, where the names of the parties were not disclosed, the *Bezirksgericht* of Albis said that where public policy was concerned, there were "considerably lower requirements" for arbitral tribunals than courts. [38]

In *C Import and Export Company v G SA* [39], the *Cour de Justice* in Geneva very closely followed the words of the case noted by van den Berg, stating that the public policy defence only applied:-

> " . . . in the presence of a violation of the fundamental principles of the Swiss legal system, which hurt the innate feelings of justice in an intolerable manner." [40]

The public policy defence has succeeded in some Swiss arbitral awards, however. In ICC Case Number 5622 of 1988, [41] the Claimant contracted to provide advice to the

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36 at p.11.
37 Van den Berg, op cit, at 365.
38 Referred to in *Yearbook Commercial Arbitration* XXIII (1998), at 754.
39 *Yearbook Commercial Arbitration* XXIII (1998), at 764.
40 op cit, at 769.
41 Reported in Arnaldez, Derains and Hascher, *Collection of ICC Arbitral Awards*, Volume 3, Kluwer, 1995, at 220.

Defendant as to how best to be awarded a construction contract with Algerian authorities. Moneys said to be due to the Claimant for the provision of advice and performance of services were not paid. The claim was defended on the basis that the Claimant had engaged in illegal activity by improperly influencing Algerian officials. The arbitrator held that Algerian law had been violated by the Claimant's activities and denied the claim. The arbitrator said:-

> "It is unanimously recognized that trading in influence is a practice which must be sanctioned . . . the law of Algeria lays down a general principle which must be respected by all legal systems wishing to fight corruption. This is why the violation of this Law, which concerns international public policy, is contrary to the notion of morality based on Art. 20(1) CO, which is part of Swiss public policy." [42]

It is difficult to say what the impact of this decision might be. The report notes that the award was annulled and that a second award "reportedly granted the claim." [43] There is no mention of the grounds upon which the award was annulled. [This case is also interesting for observations made by the arbitrator as to the circumstances when a court or tribunal might suspect the possibility of corruption. This is looked at further in Chapter VIII of the Dissertation.]

In ICC Case Number 6248 of 1990, the public policy defence was also raised. The arbitrator found that the parties had attempted to conceal the true nature of their contract. (The claimant had engaged in improper activities by extorting secret commissions.) The arbitrator held that this violated both the *Code des Obligations* and international public policy and denied the claim. [44]

(c) England

In *Westacre Investments Inc v Jugoimport-SDPR Holding Co Ltd and ors* [45], the majority in the Court of Appeal held that the application of public policy could

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42 at 230. ("CO" stands for *Codes des Obligations*.)
43 at 221.
44 Arnaldez et al, op cit, at 239.

involve a balancing act; where, for example, a party sought to resist enforcement on the basis of illegality in the underlying contract, this was something which must be counterbalanced against the competing public policy issue of the finality of awards.

Developing States

The issue of arbitrability for developing States was discussed in Chapter VI. Article V.2(b) is also an issue, for analogous reasons. In materials prepared for the American Arbitration Association shortly after the accession to the New York Convention by the United States, Straus referred to the public policy defence as providing:-

> ". . . one important loophole, which may long be troublesome". [46]

Straus continued:-

> "This of course gives wide latitude to the local courts, especially in large cases which can affect the national interests." [47]

If, for developing States, arbitrability is an issue because of perceived national interest, then, so too must be public policy and the enforcement of awards. It might, however, be more difficult for local courts to refuse enforcement than to deny arbitrability at an earlier stage of proceedings.

Comments

The dominant theme in the jurisdictions referred to is that awards must be enforced unless the most exceptional circumstances apply.

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45 [1999] 3 WLR 811, at 835, 836.

46 Straus, "Arbitration of Disputes Between Multinational Corporations", in *New Strategies for Peaceful Resolution of International Business Disputes*, American Arbitration Association, Oceana, 1971, 109 at 114.

47 op cit, at 115.

This is manifested in different ways – there might be a reliance on the objects of the New York Convention (it is "pro-enforcement"), or preference is given to one aspect of public policy (finality) over other aspects (illegal contracts ought not to be enforced).

It will be argued in Chapter VII that the narrowing of the public policy defence in these ways is not appropriate.

CHAPTER VII

DOES *PARSONS & WHITTEMORE* REPRESENT AN APPROPRIATE APPROACH TO PUBLIC POLICY?

> " . . . *by neutralizing one the Convention's seven defences, Parsons has knocked out one of the Convention's keystones.*" [1]

Is it possible to restrict public policy?

Any decision to limit the application of public policy is of course, itself a policy decision. It will be suggested that any such decision is, however, impermissible, as being at odds with the very conception of public policy itself.

Did the Court in *Parsons & Whittemore* adequately consider the role of public policy?

In *Parsons & Whittemore*, the United States Court of Appeals (Second Circuit) referred to two articles which discussed the public policy defence, noting that one commentator (Quigley) had suggested that the defence be accorded a wide application, whilst the other (Contini) argued for a narrow application. [2]

Quigley observed that, at the 1958 UN Conference, there was debate over whether to include the words "or with fundamental principles of the law (*ordre public*)" after "public policy" in Article V.2(b). To do so would have "carried over the language of Article 1.(e) of the Geneva Convention." [3] The decision not to include those words, Quigley concluded, may be read as a "broadening of the definition" of public policy.

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1 Bouzari, op cit, at 217.

2 Quigley, "Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral awards", op cit, at 1070, 1071; Contini, "International Commercial Arbitration", 8 *American Journal of Comparative Law* (1959), 283, at 304.

3 Quigley, op cit, at 1070.

Contini had noted the same debate - but stated that the omission of the words "liberalized" Article V.2(b) "in favour of the plaintiff". [4]

The Court said that the more probative inferences on interpretation, however, were to be drawn from the history of the New York Convention as a whole. [5] The Convention had a "pro-enforcement bias" and that pointed towards a narrow reading of the public policy defence. The Court continued:-

> "An expansive construction of this defence would vitiate the Convention's basic effort to remove pre-existing obstacles to enforcement."[6]

The Court then noted commentary by Straus and Reese [7]. Straus referred to Article V.2(b) as "an important loophole", which gave "wide latitude" to local courts, especially in "large cases which can affect national interests." [8] Reese said that the defences in the Convention "were unexceptional except for the 'public policy' escape hatch." [9]

The Court was obviously concerned at the thought of "loopholes" and "escape hatches", perhaps particularly so in "large cases", as referred to by Straus.

The Court's construction of Article V.2(b) was designed to close these off.

The Court also referred to (but without discussion) the decision of the Court of Appeals of New York in *Loucks et al v Standard Oil Company of New York* [10]. In that case, the Court considered an application by the spouse of a person killed in an highway incident in Massachusetts to bring an action in New York against the employer of those responsible. A Massachusetts statute gave the plaintiffs a right of

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4 Contini, op cit, at 304.
5 It is suggested that Quigley's view is, as a question of construction, to be preferred.
6 *Parsons & Whittemore*, op cit, at 973.
7 In *New Strategies for Peaceful Resolution of International Business Disputes*, op cit; Straus, op cit; Reese, "Digest of Proceedings of International Business Disputes Conference", April 14, 1971, at 191.
8 Straus, op cit, at 115.
9 Reese, ibid.
10 224 NY 99 (1918).

action. In delivering the opinion of the Court, Cardozo J noted that the rules of private international law applied. [11] His Honour stated that where a plaintiff has a right which has accrued somewhere else, the approach of the courts should be as follows:-

> "The plaintiff owns something, and we should help him get it . . . unless some sound reason of public policy makes it unwise for us to lend our aid." [12]

His Honour noted that the application of public policy, however, had to be based on certain considerations:-

> "The courts are not free to refuse to enforce a foreign right at the pleasure of the judges, to suit the individual notion of expediency or fairness. They do not close their doors unless help would violate some fundamental principle of justice, some prevalent conception of good morals, some deep rooted tradition of the common weal." [13]

As noted, the Court in *Parsons & Whittemore* did not discuss this case. The reasons for that can only be surmised. Certainly, a discussion of the judgment of Cardozo J would have provided an interesting counterpoint to the reasoning of the Court of Appeals.

Comments

It is submitted that there was little justification in *Parsons & Whittemore* (and in *MAN Gutehoffnungshütte* which, as noted in Chapter VI, appeared to take *Parsons & Whittemore* even further) for the application of such a stringent test. When the historical basis of public policy is considered, it is clear that public policy was not intended to have a peripheral role. It is central to the application of the law, in both common law and civil law jurisdictions.

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11 op cit, at 102.
12 op cit, at 110.
13 op cit, at 111.

Winfield points out that it is not possible to "fence in" public policy. [14] There is a clear duty on courts to apply public policy and that duty cannot be discharged by restricting the scope of public policy, as the law simply cannot develop if this happens. The law itself cannot be fettered.

Public policy is the constantly available *benchmark for judicial legislation* and this cannot be restricted to something applied only in extreme cases.

To restrict public policy, consequently, is to effectively negate it - and to do that is an abrogation of duty for both courts and arbitrators. Surely this was not the intention of the drafters of either the New York Convention or UNCITRAL Model Law.

During the debates on the UNCITRAL Model Law [relevantly, in relation to Article 34(2)(b)(ii)], Bonell stated that:-

> " . . . the purpose of the subparagraph was to make it clear that, in addition to the reasons set out in the preceding subparagraphs [*ie, the specific grounds for recourse*], there was a more general limitation beyond which an award could not go." [15]

In other words, the public policy defence is the medium by which general principle is applied. This accords with the traditional view of public policy.

When the observations of Lauterpacht J in the *Guardianship Case* [16] are also considered, it is clear that the ability to utilise the "safety valve" of public policy is so crucial to private international law, that it could not function without it.

The reality is, however, that this is not happening:-

> " . . . the courts have given the public policy defence so narrow a construction that it now must be characterized as a defence without meaningful definition. This leaves the defence pragmatically useless if not altogether nonexistent." [17]

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14 see Chapter IV.

15 Holtzmann and Neuhaus, op cit, at 979.

Van den Berg notes concerns that the Courts, particularly those of the United States, may have gone too far in limiting the application of public policy to the extent that they have. It has been suggested that this is counter-productive - if "blind lip service" is paid to international commercial arbitration, then its effectiveness may be devalued. Parties may be reluctant to resort to arbitration, if the "catch-all" defence under Article V.2(b) could not protect the integrity of arbitral processes. [18]

Van den Berg dismisses such concerns, stating that the application of public policy is akin to the swinging of a pendulum. He states that the point has not yet been reached where arbitration has become devalued because of the limitation on public policy considerations. Interestingly, however, van den Berg notes that such a result is a possibility, if the limitation is applied blindly. He continues, however, by stating that this possible danger does not of itself justify removing or rejecting the limitation. [19]

With respect, that seems illogical. If there is a danger in the present approach, then should that not be tempered somewhat lest the apprehended devaluation of arbitration occurs?

Public policy must be afforded its proper role within the law - this is as important to the functioning of the New York Convention as the recognition of its "pro-enforcement bias". To accord a proper role to public policy does not negate the "pro-enforcement" approach of the New York Convention (and which also should apply to the UNCITRAL Model Law).

The Convention itself recognises that public policy considerations may be applied. In *Loucks v Standard Oil*, Cardozo J said that the Courts looked to assist a plaintiff who had accrued a foreign right, subject to the application of consistent, soundly based public policy principles. [20] This was the equivalent of saying that the Courts should be "pro-enforcement" in relation to a right such as an arbitral award.

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16 op cit, at 270, et seq.

17 Junker, "The Public Policy Defence to Recognition and Enforcement of Foreign Arbitral Awards" 7 *California West International Law Journal* (1977), 228, at 245.

18 Van den Berg, op cit, at 367.

19 op cit, at 368.

20 op cit, at 110 et seq.

The decision in *Parsons &Whittemore* is, of course, itself the application of public policy. In effect, the Court of Appeals (Second Circuit) said - "this is how we will apply public policy." The decision is, however, at odds with the very essence of public policy. Public policy cannot be fettered - it is difficult to think of any other fundamental conception of law which has been attacked in this way.

The principal result of such an approach to the application of the law is that many social interests become ignored. As Stone noted, no one social interest is inherently better than another - all have to be taken into account. [21] A reading down of public policy in order to ensure that one set of values only is taken into account, negatives the application of the law itself.

In 1968, in a letter to President Johnson recommending the adoption of the New York Convention by the United States, the then US Secretary of State assured the President that the public policy defence afforded a "substantial safeguard" against "the misuse of the arbitral process." [22]

It is perhaps ironic that the Secretary of State, in contradistinction to commentators such as Straus and Reese, saw the public policy exception in a positive light. It is even more ironic that United States' courts have brought about the negation of that very safeguard.

[The consequences of the reading down of public policy in Parsons & Whittemore are discussed further are pp. 226-227.]

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21 op cit, at 489.

22 Letter of Submittal from United States Secretary of State Katzenbach to the President, April 13, 1968, reproduced in *New Strategies for Peaceful Resolution of International Business Disputes*, op cit, 1971, at 6.

PART III

CASE STUDIES

GLOBALISATION AND COMMERCIAL ARBITRATION

RECOMMENDATIONS

CHAPTER VIII

CASE STUDY - *WESTACRE INVESTMENTS*

> "*Today, corruption is internationally recognised as a major problem in society, one capable of endangering the stability and security of societies, undermining the values of democracy and morality, threatening social, economic and political development . . .*
>
> *With growing globalization . . . the international dimension of corruption gains in significance.*" [1]

Applying the wrong public policy?

It will be suggested that the decision in this case illustrates a problem which perhaps is not readily apparent at first glance. The Courts [2] applied a public policy principle, but a narrowly fashioned principle, inappropriate to the circumstances.

By way of background - the significance of the decision may be better understood by putting it in the context of international concerns over commercial corruption, and linking that to the operation of the New York Convention.

Background - commercial corruption – a significant issue

Commercial corruption has become a serious global problem.

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1 OECD Anti-Corruption Division *wwwl.oecd.org/daf/nocorruption/initiatives*.

2 The English High Court of Justice and the Court of Appeal for England and Wales.

Formal steps aimed at eradicating corruption have been taken at Government level and by international bodies such as the UN, the OECD and the WTO:-

- The UN, on 16 December 1996, adopted the *Declaration against Corruption and Bribery in International Commercial Transactions*, under which Member States are committed to take action against "all forms of corruption, bribery and related illicit practices".

- The EU members are signatories to the *Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of the Member States of the European Union* which addresses bribery of EU officials.

- The OECD opened for signature its *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* in December 1997. This Convention addresses the issue of the corruption in the public arena. Signatories must ensure that their national laws create the specific offence of bribery of foreign public officials. [3] Additionally, the OECD's *Guidelines for Multinational Enterprises* prohibit the rendering of bribes to public officials.

- In February 1999, the inaugural meeting of the *Global Forum on Fighting Corruption* was held in Washington, attended by delegates from approximately 90 countries. [4] A second meeting was held in 2001, at the Hague.

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[3] As at 10 October 2002, 34 countries had deposited instruments of ratification of the Convention, including the United Kingdom. The United Kingdom's implementing legislation (the *Anti-terrorism, Crime And Security Act* 2001) did not come into effect until 14 February 2002.

[4] Details at http://usinfo.state.gov.

- The WTO has identified corruption and bribery as significant obstacles to transparency in economic policy-making. [5]

- At private sector level, the ICC has issued *Rules of Conduct to Combat Extortion and Bribery in International Business Transactions*, which individual corporations may voluntarily endorse.

The nature of corruption

It has been suggested that global corruption is "roughly a pyramid of three levels." [6] At the top lies business bribery of foreign officials (usually involving Western corporations and public officials of less developed States), in relation to arms sales and development contracts so as to obtain concessions or infrastructure contracts; next is money laundering (mostly involving illicit receipts from the drug trade) and finally, domestic political and commercial corruption. [7]

The effects of corruption

Corruption is not simply a question of illegality. The WTO notes the highly distortionary economic effects of such practices in areas such as public investment. This is also noted in a World Bank report:-

> "Corruption is likely to be costly in terms of economic efficiency . . . Official corruption distorts the market and its implicit price mechanisms . . ." [8]

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5 Drabek and Payne, *The Impact of Transparency on Foreign Direct Investment*, Staff Working Paper, World Trade Organization Economic Research and Analysis Division, August 1999, at 7.

6 Windsor and Getz "Symposium Fighting International Corruption & Bribery in the 21st Century: Multilateral Cooperation to Combat Corruption: Normative Regimes Despite Mixed Motives and Diverse Values" 33 *Cornell International Law Journal* (2000) 731, at 751.

7 op cit, at 751.

8 Buscaglia and Dakolias, *An Analysis of the Causes of Corruption in the Judiciary*, Legal and

Nor are the effects of corruption merely economic:-

> "It [*corruption*] threatens development, safety, social fairness, the environment and stability in many different ways." [9]

Clearly, commercial corruption is a serious problem. It is found at the highest levels:-

> "Corruption is an intrinsic part of the way the state operates in many countries." [10]

Consequently, corruption is culturally and socially entrenched in many countries. [11] It is found both in the public arena and in private business dealings. [12]

It is also an issue which, despite the activities of the international bodies referred to above (ie, the UN, the OECD, the World Bank) will be difficult to eradicate for a number of reasons (including institutional and cultural factors). The extent to which corruption is entrenched is an enormous obstacle to reform. An added difficulty is that certain Western States permit bribery payments to be tax deductible (although that is now changing, with some countries reversing previous practice). With such an attitude, however, the official Western line against corruption is severely weakened.

How is consideration of corruption relevant to a discussion of the New York Convention?

It was argued in Chapter VII that cases such as *Parsons & Whittemore* have meant that the public policy defence within the Convention has become virtually ineffective.

Judicial Reform Unit, Legal Department, World Bank, 1999, at 1 and 3.

9 Bottelier, *Remarks for International Symposium on the Prevention and Control of Financial Fraud*, Beijing, October 19, 1998. (Obtained from www.icclr.law.ubc.ca.)

10 Buscaglia and Dakolias, op cit, at 1.

11 Buscaglia and Dakolias, op cit, at 3.

The result has been not only a breach of duty on the part the Courts, but an important weapon against commercial corruption is in danger of being discarded.

There have been instances of courts being requested to invoke the public policy defence because of alleged corruption in the parties' dealings. It is submitted that the correct approach to this issue was taken in *European Gas Turbines SA v Westman International Ltd* [13], where the *Cour d'Appel* of Paris said that the trafficking of bribes was against the public policy of France and violated morality in international commerce, "so much so", that a prohibition on the trafficking of bribes was "a general principle of law."

Such a robust approach has not always been evident, however.

Before looking at the case studies in more detail, it is worth noting commentary from one of the Swiss awards noted in Chapter VI. [14] The arbitrator relied on *dicta* from some United States decisions in making observations regarding signs of the possible existence of corruption. These included - the intervention of an "agent", "sponsor" or "consultant" who was resident in the jurisdiction other than the place where the services were to be rendered; the service provider generally not being submissive to the laws of that place; the fees payable being disproportionately large in relation to the actual work to be performed; and the real relationship between the parties being disguised. [15]

As noted, this award was annulled, but is submitted that these observations are of some relevance, particularly in light of the facts of the case to be discussed below.

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12 ibid.
13 Yearbook Commercial Arbitration XX (1995) 198.
14 ICC Case Number 5622 of 1988, in Arnaldez *et al*, op cit.
15 op cit, at 230-232.

Westacre - High Court

The case of *Westacre Investments Inc v Jugoimport-SPDR Holding Co Limited and ors* [16] involved the sale by the defendants (a Yugoslav state enterprise) of military equipment to Kuwait. Prior to the signing of the contracts, the defendants had been made aware of a Kuwaiti Ministry of Defence ("MOD") circular, in which it was stated that the defendants should not engage any agents or intermediaries for the making of the contracts. Also during the course of the negotiations, the defendants encountered a senior Kuwaiti Minister, who had access to internal information of the MOD.

The Minister advised the defendants to ignore the MOD advice and that they should appoint the plaintiffs (a company based in Panama) as their exclusive consultant. The defendants did so.

The sale went ahead, with the Minister subsequently informing the defendants that "his group" had procured the contracts in favour of the defendants "against the opposition." [17] The defendants, however, cancelled the consultancy agreement with the plaintiffs, without paying the agreed fees.

The parties went to an ICC arbitration in Paris (under Swiss law) at which the arbitrators found for the plaintiffs. The plaintiffs then sought to enforce the award in England. The defendants claimed that the contracts underlying the award were illegal. It was contemplated that the consultants would use "personal influence" to procure the contracts, that this would be done without Kuwaiti government officials knowing that payment was involved and that it was intended to bribe Kuwaiti officials. Accordingly, public policy required that the award not be enforced.

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16 [1998] 4 All ER 570.
17 at 575.

The defendants relied on an affidavit, which Colman J referred to as the "MM affidavit". The MM affidavit offered an analysis of the transactions between the parties and the deponent, MM, concluded that the plaintiff company was a vehicle for interests associated with the Minister. MM further asserted that the only inference which could be drawn from the fact of the "unusually high commission" to be paid to the plaintiffs was that this was for "illegitimate purposes". [18]

No evidence was led in reply. Colman J said that it was assumed that the inferences raised in the MM affidavit were proved. [19]

His Honour, however, did not allow the defendants to reopen their case. The issue of illegality "by reason of corruption" had been raised before the arbitrators (a high calibre ICC panel) and "duly determined" by them. [20] His Honour said that the application to reopen their case on the basis of illegality, when it was open to the defendants to have adduced evidence on this point before the arbitrators, was "clearly in conflict with the principles of issue estoppel." [21] In its considerations, the Court had to balance:-

> " . . . whether the public interest in preventing the enforcement of corrupt transactions outweighs the public interest in sustaining the principle of nemo debit bis vexari which underlies issue estoppel." [22]

Colman J concluded (most unfortunately, it will be argued below) that, whilst there was growing concern over the "precedence of corrupt trading practices" (and His Honour also noted that at that very time that His Honour's judgment was being delivered, various governments, including that of the United Kingdom, were signing the *OECD Convention on Combating the Bribing of Foreign Officials in International*

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18 at 576.
19 ibid.
20 at 598.
21 at 597.
22 ibid.

Transactions) [23] "few would consider" that commercial corruption stood on the same scale as (for example) drug-trafficking. [24] Consequently, the policy of sustaining finality in awards prevailed and His Honour held that the award should be enforced.

The case went to the Court of Appeal. Shortly before the appeal was heard, the Court of Appeal decided *Soleimany v Soleimany* [25]. The parties in that case had originally agreed that the plaintiff was to arrange for carpets to be exported from Iran to the United Kingdom and other places, where they would be sold by the defendant. These exports were illegal under Iranian law. The plaintiff complained that the defendant had not provided a share of the proceeds. The parties went to arbitration in the rabbinical Court, the *Beth Din*. The *Beth Din* applied Jewish law, under which the illegality of a contract does not affect the rights of the parties - *inter alia*, an action for damages may still lie. The *Beth Din* awarded damages to the plaintiff.

The Court of Appeal refused enforcement of the award. The Court noted that the *Beth Din*, unlike the arbitral panel in *Westacre*, found that the contract was illegal. Whilst this did not affect the plaintiff's right to compensation under Jewish law, Waller LJ (delivering the judgment of the Court) said that English public policy was against enforcement. His Lordship distinguished the *Westacre* case but emphasised some disagreement with the propositions as put forward by Colman J. His Lordship said that courts should not be restricted, in appropriate cases, from making inquiry into the issue of illegality. This was so even where the issue had been raised before the arbitrator.

Westacre - Court of Appeal

Rather a different view of the background issues was taken in the Court of Appeal. Waller LJ noted that the appellants had not pleaded the allegation of bribery before

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23 at 593.
24 at 598.
25 [1998] 3 WLR 811.

the arbitrators, but, nonetheless, their counsel had raised the issue in opening the case before the panel. His Lordship quoted from the award:-

> ". . . it is up to the defendant to present the fact of bribery . . . If the defendant does not use it in his presentation of facts an arbitral tribunal does not have to investigate . . . It is exclusively the parties' presentation of facts that decides in what direction the arbitral panel has to investigate." [26]

If the extract from the award reproduced by Waller LJ was the extent of the panel's consideration of the bribery issue, it is difficult to see how this could have been a "due determination". On the part of the arbitral panel, it seems an extremely narrow position was taken - because an allegation was not formally pleaded, it could not be dealt with *at all*. There was seemingly no consideration as to whether any amendment to the presentation of facts was possible, either with or without an adjournment.

Waller LJ also noted that the arbitral proceedings went to the Swiss Federal Tribunal on appeal. The Federal Tribunal indicated that the appeal was without merit, being no more than a "feckless criticism" of the arbitrators' findings of fact. [27] The Federal Tribunal also stated that its role was restricted in any event, in that it could only base its decision on the facts as found by the arbitrators.

It is difficult to know precisely what happened before the arbitrators - why the appellants did not formally plead bribery. The issue having been raised (even informally), however, it is hard to see why such a narrow position was taken by the arbitrators. It seems, it is submitted, an abrogation of duty not to have considered such an issue.

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26 Reproduced in judgment of Waller LJ, [1999] 3 WLR 811, at 815, 816.
27 ibid.

The first argument of the appellants was what Waller LJ called the "*Lemenda* point". This was based on the claim that the contract was illegal under Kuwaiti law, and consequently, any award based on it could not be enforced. His Lordship dismissed this point, distinguishing *Lemenda* on the basis that the proper law of the contract was Swiss law, and a contract to utilise personal influence was not illegal under Swiss law.

The second point was as to whether the appellants could now amend their case to allege that the respondent (via its witnesses) had given perjured evidence before the arbitrators. In this context, Waller LJ noted the anomalous position with the enforcement of foreign judgments, in that they may be attacked on this point, even if the issue of perjury had been raised before the foreign court hearing the matter. [28] His Lordship concluded that awards should not be treated in the same fashion as judgments. There was "no good reason" why the appellants did not go on appeal in Switzerland on this point, and consequently, they should not be allowed to amend.

Waller LJ then considered whether the facts could be reopened, on the basis of allegations contained in the MM affidavit. (There was no reference to Colman J's remarks as to the inferences contained in the MM affidavit having been established. Ultimately, Waller LJ did not take it that the matters covered in the MM affidavit were proved, although His Lordship did regard the MM affidavit as having certain credibility, and as raising serious issues). [29]

His Lordship referred to the Court's recent decision in *Soleimany v Soleimany* [30], in which the Court (Waller LJ having given the judgment) noted the tension between two competing public interests – that awards of arbitrators should be respected, so that

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28 Usually, for a judgment to be reconsidered on the basis of new evidence, certain tests must be met – firstly, the new evidence sought to be introduced must not have been available at the trial; next, it must be sufficiently material, so that it might have influenced the court; and, finally the evidence must be apparently credible.

29 At 834, Waller LJ said " . . . *if* the facts in MM's affidavit are correct . . ."(emphasis added). Colman J at first instance had said – " . . . both the primary facts and the inferences of fact drawn by MM in that affidavit are to be assumed to be proved." (at 576).

30 Waller LJ in *Soleimany*, op cit, at 822 et seq.

there was an end to litigation, and the interest that illegal contracts ought not be enforced.

His Lordship continued to the effect that, in *Soleimany*, the Court had noted (*obiter*) that in an appropriate case a Court may inquire into alleged illegality even where the arbitrators had concluded that there was none. The position was similar to (exceptional) cases where the courts had not permitted a party seeking enforcement of a judgment to assert estoppel against a defendant who had failed to raise fraud in previous proceedings involving the same subject matter. [31]

The principle underlying these authorities was that the court would restrain the plaintiff where there was raised " . . . 'argument on principles of public policy which are of the greatest importance'." [32]

His Lordship summarised the position as follows:-

> "The Court is in this instance performing a balancing exercise between the competing public policies of finality and illegality; between the finality that should prima facie exist particularly for those that agree to have their disputes arbitrated, against the policy of ensuring that the executive power of the English court is not abused. It is for these reasons that the nature of the illegality is a factor, the strength of case that there was illegality is also a factor, and the extent to which it can be seen that the asserted illegality was addressed by the arbitral tribunal is a factor." [33]

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31 His Lordship referred to *Arnold v National Westminster Bank plc* [1991] 2 AC 93, *Kok Hoong v Leong Cheong Kweng Mines Limited* [1964] AC 993 and *E D & F Man (Sugar) Limited v Yani Haryanto* (No 2) [1991] 1 Lloyd's Rep 429, at 882 *et seq.*

32 op cit, at 833.

33 ibid.

Accordingly, the issue becomes a question of degree, not only as to the seriousness of the conduct impinged, but the extent to which the arbitrators dealt with the matter, if at all.

Waller LJ then stated that he disagreed with Colman J as to "the appropriate level of opprobrium at which to place commercial corruption." The principle that against enforcing a corrupt bargain of the nature of the contract between the parties in this particular case fell into the category of "automatic refusal" of enforcement as enunciated by Phillips J in *Lemenda*. This is based:-

> " . . . on public policy of the greatest importance and almost certainly recognised in most jurisdictions throughout the world." [34]

Further, it was important that English courts are:-

> " . . . not seen to be turning a blind eye to corruption on this scale". [35]

His Lordship continued that, if unanswered, the case made out by the MM affidavit:-

> ". . . would be conclusive against Westacre being entitled to enforce the agreement and thus the award . . .". [36]

His Lordship also noted that it was apparent that the arbitrators had not had an opportunity to consider the case as it was now presented it was certainly possible, His Lordship had earlier noted (in a general sense), that parties may disguise illegality. [37] It was enough that a credible case concerning a serious issue had been advanced.

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34 op cit, at 834.
35 ibid.
36 ibid.
37 op cit, at 830.

Whilst some cognisance must be had of what had taken place in the arbitration, the findings by the arbitrators were not conclusive. The Court could look at the totality of the situation, and intervene if this was warranted. His Lordship concluded that the award should not be enforced.

The majority (Mantell and Sir David Hirst LJJ) agreed with Waller LJ on both the *Lemenda* and application for amendment points, but not on the reopening of the case. In a brief judgment, Mantell LJ said that it was sufficient that the arbitrators had considered the issue of alleged illegality. His Lordship doubted the usefulness of the Court embarking on an inquiry; even if it did, any preliminary investigation would have led to the same conclusion – that the application to reopen should be refused. [38] Sir David Hirst agreed, adding that His Lordship believed that the trial judge had "struck the correct balance" by giving "ample weight to the opprobrium attaching to commercial corruption." [39] It seems from this that Hirst LJ did not necessarily agree that corruption was not involved, but simply took the same view as Colman J, that corruption was not so terribly serious.

Comments

It is submitted that the position taken in the High Court and by the majority in the Court of Appeal was quite inappropriate. In the circumstances, it is questionable whether the issue of finality should have been given more than cursory consideration.

The question was put by Colman J in the context of issue estoppel - the arbitrators had determined the matter. Whilst courts have held that the doctrines of *res judicata* and issue estoppel apply to arbitral awards, there should be some caution in applying them, however, to awards.

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38 op cit, at 835.
39 op cit, at 836.

There are obvious differences between court proceedings and arbitrations. Arbitrators do not operate under the same transparency as judges and their procedures for taking evidence and establishing facts may be not as stringent as those of courts. Further, court judgments are matters of public record, setting out how the rights of the parties have been determined. The reasons behind awards are not made public. [40]

All of these factors lessen the degree of certainty that might be ascribed to awards, as opposed to court judgments. Further, even with court judgments, the application of *res judicata* and issue estoppel is not always easy:-

> "The quagmire that exists for the judicial system is how to balance the competing interests of finality and certainty against society's concerns for justice and fairness." [41]

If there are difficulties with balancing these interests in respect of judgments, which, for the reasons set out above, might be said to be more "certain" than awards, then this must militate against too strictly applying the principle of "finality" to awards.

In any event, what is behind the desirability of "finality"? The factors referred to above:-

> " . . . cast doubt on the assumption . . . that the second hearing on an issue is likely to be a waste of social resources." [42]

Colman J (in *Westacre* at first instance) had referred to the maxim, *nemo debit bis vixari*, that there should not be two hearings on essentially the same issues. In

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40 Shell, op cit at 658 and 659.

41 Richards, "Richards v Jefferson County: The Supreme Court Stems the Crimson Tide of Res Judicata", 38 *Santa Clara Law Review*, 691, at 742.

42 Shell, op cit, at 660.

Westacre, however, there was some doubt as to whether the issue had been "tried" at all before the arbitrators.

It is suggested that in the context of an enforcement of a foreign award, where the issues may not be tried *de novo*, the court should consider whether and to what extent the issue was raised before the arbitrators and the cogency of the evidence now being brought forward. [43] If that evidence is cogent, then the courts ought to inquire into it. The principles of res judicata and issue estoppel may be relevant if it is clear that the arbitrators did consider the issues fully *and* that the evidence sought to be brought at the enforcement stage is either not new or would add little to the defendant's case. This process should alleviate concerns over fairness to the party against whom corruption is alleged.

Finality may be largely based on concerns of efficiency, but the problem of corruption involves much more. The pronouncements of the UN, OECD and EU referred to at the start of this Chapter are sufficient evidence of that.

The following has been noted in the context of the arbitrator's duty, but could apply with equal effect to courts, in enforcement actions:-

> "Corruption is a plague; this should in and of itself justify the application of the law of the state which is concerned . . . and it should be so, I submit, even if . . . corruption has not been proven on the facts." [44]

Mayer suggests that it is sufficient that there is evidence of corruption. Obviously, there must be some test involved - the evidence must be cogent, or "reasonable", or otherwise sufficient to justify the court finding that an agreement is void on the grounds of illegality. It is submitted, however, that it is correct to say that proof is not necessary, so long as cogent reasons exist.

[In this context, the arbitrator's observations in ICC Case 5622 of 1988 [45] (referred to at the beginning of this Chapter) regarding indicia of possible corruption become rather interesting. In *Westacre*, firstly, the claimant was a consultant; was based in a jurisdiction other than the one where the services were to be performed; and also received what was described as an unusually high commission. These factors are not proof in themselves, but could have alerted the arbitrators and the Courts to take a closer look at the circumstances.]

The effect of the approach in *Westacre*

To say that one aspect of public policy ought to have been chosen over another might seem to be largely a subjective appraisal of what is considered as being "in the public good." When the import of the decision in *Westacre* is considered, however, it is submitted that it was objectively wrong to choose a principle which elevated concerns of efficiency over the opportunity, rather, the duty, to strike down a corrupt agreement.

If finality becomes the dominant consideration, then all other aspects of public policy will effectively be excluded. To do as the courts (with the exception of Waller LJ) did in *Westacre* is ultimately analogous to the approach of the United States Court of Appeals (Second Circuit) in *Parsons & Whittemore*.

Public policy is placed on a narrow footing - which, whilst a policy decision in itself, does not accord with the concept that public policy has a fundamentally important role within the law.

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43 This, essentially, is the position taken by Waller LJ in *Westacre*.
44 Mayer, op cit, at 247.
45 op cit.

Public policy is about applying high principle in the public interest, not ensuring the maximum degree of efficiency in commerce to the exclusion of almost all else.

Efficiency and certainty are, of course, desirable, but that is all they are. They are not sacrosanct principles.

Corruption ought to be regarded in the same light as fraud and with the same consequences. If "fraud unravels all", then agreements which envisage corrupt behaviour (irrespective of how that is masked), should also be treated as void.

One might also question whether the glossing over of corrupt activities can truly be efficient in the long run, given the potential for corruption to distort and destabilise economies.

"Characterisation"

It has been suggested by one commentator that the question of "characterisation" of the relevant activity undertaken by the parties becomes most important. [46] For instance, with *Soleimany*, it might be said that the activity was properly seen as "smuggling carpets", rather than trade or commerce; in *Westacre*, the activity centred around "lobbying" and "personal influence", rather than bribery. [47]

Whilst Meltz's suggestion is logical, it does not extend to recognising that it is essential that the activity be *properly* characterised, not glossed over. In *Westacre*, there was some discussion as to whether the plaintiffs were intended to offer bribes, or "exercise personal influence", an activity which apparently falls short of bribery. [48]

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46 Meltz, "Public Policy and Illegality: The Westacre Legacy", *The Vindobona Journal of International Commercial Law and Arbitration*, Volume 4, Issue 1 (2000), at 80.

47 Meltz, op cit, at 87.

48 It might be noted that, in *Lemenda*, Phillips J said that "exercising personal influence", particularly where the target of the influence is unaware that the influencer is being rewarded

If public policy is to be applied to combat corruption, there must not be a way of defeating that via the glossing over of the conduct involved.

Parties should not be allowed to waive objections to corruption

In this context, mention might be made of another case where corruption was raised - *AAOT Foreign Economic Association (VO) Technostroyexport v International Development and Trade Services Inc.* [49] The corruption alleged was not to do with the parties' contract, but in the arbitral tribunal itself. Some time before the arbitration commenced, in an apparent effort to "test" the integrity of the arbitrators, an agent of the appellant had approached the Secretary of the arbitral tribunal to see if the tribunal "could be 'bought' ". The response seemingly was in the affirmative. The agent then carried out some "negotiations", which subsequently lapsed without any payment being made. The arbitration was heard and the appellant was ordered to pay the appellee some $200M in damages. The appellee attempted to enforce the award in the United States. The appellant claimed that the tribunal had been corrupt and raised the public policy defence. The court at first instance had found that the appellants had initiated the discussions and that they had not established that the tribunal had been in fact corrupt in the particular hearings. In the circumstances, they consequently waived their rights to the defence. The Court of Appeals (Second Circuit) agreed, stating that previous authority established that where a party had knowledge of facts possibly indicating bias or partiality on the part of arbitrators, that party could not remain silent. The Court said:-

> "The law of waiver controls the outcome of this appeal. It is undisputed that IDTS had knowledge of concrete facts possibly indicating the corruption of the Arbitration Court . . Despite this knowledge, IDTS remained silent. Accordingly, it now cannot object to the award on this basis." [50]

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for his or her efforts, is "unattractive whatever the context" (at 461).

49 139 F.3d 980 (Second Circuit, 1998).

50 op cit, at 982.

The Court of Appeals for the Second Circuit saw the issue as one of waiver. It does seem that there was little or no evidence as to the actual corruption of the arbitrators during the course of the arbitration. If such evidence was available, however, it is submitted that waiver is not an appropriate basis for dealing with the issue of corruption. If the court were to reasonably suspect that corruption was involved, then it should investigate the matter irrespective of any "waiver".

CHAPTER IX

CASE STUDY - *SANDLINE v PAPUA NEW GUINEA* [1]

> *"At its fifty-fourth session, the Commission on Human Rights adopted resolution 1998/6 of 27 March 1998, in which, inter alia, it reaffirmed that the recruitment, use, financing and training of mercenaries were causes for grave concern to all States and violated the purposes and principles of the Charter of the United Nations."* [2]

A failure to consider public policy?

It will be suggested that this second case study demonstrates the lack of consideration of public policy issues by arbitrators when the circumstances clearly demanded that this was necessary. As with the first case study, however, some appreciation of the background to the case is necessary.

Background

Since the 1970s, the Government of Papua New Guinea ("PNG") has been involved in a dispute with land owners and others from the island of Bougainville, which forms part of PNG. [3]

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1 *Sandline International Inc v Independent State of Papua New Guinea*, International law Reports (2000), Volume 117, 552.

2 UN Commission on Human Rights, *Report of the Special Rapporteur on the question of the use of mercenaries as a means of violating human rights and impeding the exercise of the rights of peoples to self-determination*, Document E/CN.4/1999/11, 13 January 1999.

3 Bougainville was annexed by Germany in 1899 to become part of the colony of German New Guinea. Australia took control of German New Guinea in 1914. In 1921, the colony became a ward of the League of Nations, administered by Australia. After the Second World War, Bougainville became a United Nations Trust Territory, again administered by Australia. It

The origins of the dispute go back to 1964, when Conzinc Riotinto Australia ("CRA") [4] arrived "uninvited" in Bougainville to commence exploration. [5] The local people were immediately opposed to this activity. [6] After significant copper deposits had been located in an area known as Panguna, an entity called Bougainville Copper Limited ("BCL") was formed to exploit these deposits. [7]

The local people, however, were hardly to benefit at all from the mine's operations, which, at one stage, was the second largest open-cut mine in the world. [8] Shortly after CRA established that significant mineral deposits existed, the then Australian Minister for Territories, Charles Barnes, made it clear that to the local peoples that, whilst "astronomical riches" lay in the ground, their share of the exploitation would amount to no more than compensation for damage to property and livelihood, plus an "occupation fee" of $2 per acre. [9] Between 1972 and 1989, the landholders of Bougainville received only 1.4% of the wealth generated by the mine. [10]

The people of Bougainville consequently had a number of grievances over the operation of the mine. Another significant issue is that the island's inhabitants (who see themselves as culturally distinct from other groups within PNG) are seeking independence from PNG. [11]

The dispute escalated into armed conflict, the Bougainville Revolutionary Army ("BRA") being formed in 1987. In 1989, BCL were forced to close down the mine.

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became part of PNG when PNG attained independence in 1975.

4 CRA had been formed in 1962 by the merger of the Australian interests of two United Kingdom entities -Consolidated Zinc Corporation and Rio Tinto Company (source - www.riotinto.com).

5 Griffin, in May and Spriggs (eds), *The Bougainville Crisis*, Crawford House Press, 1990, at 8.

6 Griffin Nelson and Firth, *Papua New Guinea A Political History*, Heinemann Educational Australia, 1979, at 151.

7 CRA owned approximately 53% of the shares in BCL; the PNG Government had approximately 19% - Dorney, *The Sandline Affair*, ABC Books, 2001, at 246.

8 Griffin Nelson and Firth, op cit, at 150.

9 Griffin Nelson and Firth, op cit, at 151.

10 Carruthers, in May and Spriggs, op cit, at 41.

11 Griffin, in May and Spriggs, op cit, at 4.

A unilateral declaration of independence was made in 1990 and the Bougainville Interim Government formed. The PNG Government was unable to settle the issues, either by negotiation or use of armed force (which at one stage included a blockade of the island). [12]

So ineffective were the PNG armed forces that the then Prime Minister, Sir Julius Chan, went outside PNG seeking assistance in the efforts to retake the mine (which, at its peak of operation, provided some 17% of PNG's total revenue). In January 1997, after some discussions, the PNG Government entered into a contract ("Sandline Agreement") with a company called Sandline International ("Sandline"). Sandline offered what it described as "military and security services of an operational, training and support nature." [13]

[At the same time as engaging with Sandline, the PNG Government decided to buy out CRA's shareholding in BCL. Dorney notes that it was rumoured at the time that Sandline were to be given an interest in the mine, but this was denied by the PNG Government.] [14]

In the body of the Sandline Agreement, it was stated that the "primary objective" of the engagement was to render the BRA "militarily ineffective". It was further provided that:-

> "Sandline will . . . plan, direct, participate in and conduct such ground, air and sea operations which are required to achieve the primary objective."

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12 For a chronology of the events on Bougainville, see Downer, *The Bougainville Crisis An Australia Perspective,* Commonwealth of Australia, 2001, at v et seq.

13 Set out in the recitals to a document entitled "*Sandline Document - Agreement for the Provision of Military Assistance Dated this 31 January 1997 Between the Independent State of Papua New Guinea and Sandline International*", obtained on 7 March 2000 from the web site of *The Age* (theage.com.au/news) – set out in full in Appendix C to this paper.

14 Dorney, op cit, at 247.

The Sandline Agreement also provided that Sandline personnel were to be accorded full cooperation by the PNG Defence Force and that they were to be enrolled as Special Constables of (and be entitled to issue orders to members of) the PNG Defence Force. For their services, Sandline were to be paid, *inter alia*, the sum of USD18,000,000 upon the signing of the Agreement and a further USD18,000,000 within 30 days of its "team" being deployed. The Agreement was to be governed by the "Laws of England" and also provided for arbitration ("in conformity with the UNCITRAL Rules") in the case of a dispute.

The initial payment was made as agreed. As has been well documented in the media, however, the arrival in PNG of Sandline's personnel caused enormous protest and political upheaval, particularly within the PNG Defence Force. The Defence Force chief, Brigadier Singirok, was dismissed from his post by the Government. On 16 March 1997, troops and civilians rioted in Port Moresby. Parliament was laid under virtual siege. On 21 March 1997, Sandline's representatives (with the exception of the "team leader", who had been arrested and who was ejected at a later date) were forced to leave PNG. [15]

The Arbitration and the Award

Sandline subsequently demanded payment of the second instalment of USD18,000,000. The new PNG Government (a change of government having come about as a result of the Sandline affair) refused payment.

As a consequence, the parties went to arbitration.

PNG's defence to the claim stated that it was, because of the protests and political upheaval, impossible to perform the contract, which had thereby become frustrated. PNG also counterclaimed for the return of the first instalment.

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[15] Dorney, op cit, at 287 et seq.

The arbitration proceeded in stages. PNG sought to amend its defence to allege *inter alia*, that the contract was unlawful because of the operation of s200 of its Constitution. This section provides that it is forbidden to raise armed forces except in accordance with the Constitution. PNG contended that English law would not come to the aid of a contract which was illegal in its place of performance, if that place was a friendly country and the courts of that country would not enforce the contract. The *Lemenda* case (*inter alia*) was cited in support of this. PNG also pleaded that the official who had entered into the Agreement on behalf of PNG lacked the capacity to do so; further, the Agreement was void and unenforceable, being against the public policy of both PNG and England, as constituting an impermissible fetter upon various powers.

After its defence was amended, PNG dropped its plea of frustration and also discontinued its counterclaim for the return of the first instalment.

The arbitral tribunal ("Tribunal") rejected PNG's amended defence. The Tribunal stated that consideration of s200 was irrelevant. The Tribunal acknowledged the principle of public policy (based on the "comity of nations") on which PNG had based its first submission regarding illegal contracts. This was only applicable, however, the Tribunal continued, where private parties were involved. It was not applicable to cases where States were parties to contracts. An agreement between a State and a private party is an international, not a domestic, contract. In such circumstances:-

> " . . . one enters the realm of public international law and public policy wears a different aspect." [16]

The Tribunal then stated that it was:-

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[16] op cit, 560.

> " . . . an international, not a domestic . . . tribunal . . ." [17]

and consequently, the Tribunal was:-

> " . . . bound to apply the rules of international law." [18]

The Tribunal then noted that the rules of international law are part of the laws of England, which the parties had chosen to govern their agreement; and that it is a rule of international law that a State cannot rely on its internal laws as a basis for asserting that a contract to which it is a party is illegal. In this context, authorities such as *Lemenda* "must give way" to a "fundamental qualification", such qualification which is that a State:-

> " . . . cannot rely on its own internal laws as the basis for a plea that a contract concluded by it is illegal." [19]

The Tribunal noted the 1975 *Report of the International Law Committee to the United Nations* [20], in which it was stated that when considering the liability or responsibility of a State for its conduct, its "international" acts have a quite different characterisation to its domestic acts in respect of the same conduct. Even if the international acts of its officials or organs are *ultra vires*, or contrary to domestic law, the State nonetheless bears responsibility for such acts.

Whilst this point disposed of PNG's defence, the Tribunal said that there was another consideration. The Tribunal said that the *doctrine of preclusion* applied. Under this doctrine, it was stated, it is not possible for a party to deny the validity of a contract

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17 ibid.
18 ibid.
19 at 561.
20 (1975) Vol 2, *Yearbook of the International Law Commission.*

entered into on its behalf by another, where that party's conduct subsequent to execution signified consent to the contract. The doctrine is founded on:-

> " . . . considerations of good faith and conscience which underlie the basic principle of international law, *pacta sunt servanda*." [21] (original emphasis).

The Tribunal then reiterated that PNG could not rely on its internal laws to deny the validity of the Sandline Agreement. International law disregards such matters in determining the validity of the contract. Further, PNG had participated in the performance of the Agreement, by paying the first instalment and allowing Sandline's personnel entry into the country. Each of PNG's defences accordingly failed.

The Tribunal's approach

It is suggested that the Tribunal took a very narrow approach to the issue of the relevant law, and, more significantly, the Tribunal failed to consider any possible application of public policy. The Sandline Agreement involved the provision of a foreign private army (mercenaries) to a Government in order for that Government to wage war on its own citizens.

For the Tribunal, the matter came down to essentially one issue - having entered into the Sandline Agreement, PNG was obliged to honour it. It is strongly arguable, however, that, in the circumstances, consideration of other issues (including whether the Sandline Agreement ought to have been voided on public policy grounds) should have been paramount.

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[21] at 562.

What else might the Tribunal have considered?

(a) choice of law

Whilst public international law is mostly thought of as governing operations between States, it has been accepted by a number of commentators that public international law can also govern contracts between State and a private party. [22]

Where States enter commercial agreements, it would seem less likely that they would intend that public international law apply.

Whether the Sandline Agreement was a commercial agreement is perhaps debatable. Was PNG performing an essentially executive act in raising a foreign army, or bolstering its existing army? If this was the case, then this might assist the argument that public international law was the most appropriate law to be applied.

The Tribunal's view that public international law must apply to relations between a State and a private party does not have universal acceptance. In the *Aramco Arbitration* [23], the Tribunal held that public international law could not apply to the dispute, as one of the parties was not a State. In so doing, the Tribunal followed the *Serbian Loans Case*, in which it had been held that a contract that had not been made between States in their capacities as public international subjects, must be governed by a municipal law. [24] (In the *Aramco Arbitration*, the Tribunal held that the oil concession, the terms of which were the subject of the dispute, could be "split" into several parts, "to be governed by several laws." Public international law was held to govern what was termed certain "effects" of the concession where municipal law could not apply, such as matters pertaining to sovereignty and territorial waters). [25]

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22 See the discussion in Chukwumerije, op cit, at 151 *et seq*; also, Redfern & Hunter. op cit, at 106.

23 *Saudi Arabia v Arabian American Oil Company (Aramco)* (1963) ,Volume 27, International Law Reports, 117.

24 *Payment of Certain Serbian Loans Issued in France*, (1929) PCIJ Series A, No. 20, referred to in the *Aramco Arbitration*, op cit, at 165.

25 op cit, at 166 and 172.

Maniruzzaman makes the point, relying on the *Serbian Loans Case*, to state that contracts not between States as public international subjects must be governed by municipal law. Other commentators have also stated that it is certainly the case that parties in a "mixed" arbitration (to use Toope's expression), may choose a municipal system of law to govern their agreements. [26]

PNG and Sandline chose English law as the law governing their contract. The Tribunal seemingly considered that public international law applied *automatically*, as PNG was an independent State. This, it is submitted, is not justified by any rule or principle. Whilst public international law might apply to contracts involving a State on one side and a private party on the other, it is submitted that this must primarily be so as a result of party choice. There seems to be nothing to suggest that public international law applies automatically, simply because an independent State is involved. No authority was quoted by the Tribunal on this issue.

Accordingly, there does not seem to be any reason why English law should not have applied. It may be, on one view, that nothing turned on this; what if the arbitrators had decided that the part of English law which applied was those principles of international law which have been accepted into the law of England? International law would then still have been relevant. [27]

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26 Redfern and Hunter, ibid, where the authors refer to the judgment of Megaw J in *Orion Compania Espanola*, op cit, at 264.

27 There is an English statute which prohibits mercenary activity in certain circumstances – the *Foreign Enlistment Act* 1870. It forbids, *inter alia*, the preparation within the Queen's dominions, of any military expedition to proceed against the dominions of any friendly State. Even if English law had been applied, whether the Act's provisions cover Sandline's activities is difficult to say. Preparations might have taken place within the Queen's dominions; but whether being engaged by a British Commonwealth country to fight against that country's citizens is proceeding *against* the dominions of a friendly State is something on which there is seemingly no authority. (Sandline was engaged by the State itself). It may be, consequently, that even if English law applied, Sandline's activities were not caught by the *Foreign Enlistments Act*. To have applied English law may have nonetheless put the arbitration on an entirely different footing.

(b) application of the rules of international law

It is suggested that the Tribunal's approach to resolving how the relevant rules of public international law were to be applied also deserves comment. The Tribunal stated that the principles espoused in authorities such as the *Lemenda* case must give way to the rule that a State cannot rely on a breach of its internal laws on a pleading of illegality.

It is submitted that cases such as *Lemenda* are best viewed as providing an exception to the basic principle of *pacta sunt servanda*. If the norm is that contracts and agreements are to be observed, then, the exception (ie, excusable non-observance) must be based on some competing norm or principle.

The rule that prohibits reliance on a breach of internal law should not be applied as if it were of paramount force – in the context, it should have been merely one of the competing principles under consideration.

(c) application of mandatory rules

The Tribunal noted that, in international law, the public policy reflected in decisions such as *Lemenda* had to give way to the principle that a State cannot rely on its own internal laws to escape liability for its actions. As the Tribunal noted, there are authorities and statements of principle, which suggest that irregularity may not be relied on – the irregular or illegal act is still regarded as a binding act of the State.

Maniruzzaman suggests that arbitrators should consider the possible application of mandatory rules, even when a mandatory rule is not part of the law of the contract. Where a contract is governed by a particular municipal law, but has some close connection with another State, then the mandatory rules of the other State should be

considered in any arbitration. [28] The author suggests a number of circumstances in which mandatory rules derived from a legal system outside the law of the contract might be applied - for instance, if a contract is to be carried within a State, then its economic laws should apply; or, if there is other "close contact" with a State, the application may be justified "on consideration of the circumstances." [29] A further example could be where, depending on the final outcome of the arbitration, it might be thought that it was possible for the award to be enforced in a particular State.

Gaillard and Savage also refer to the application of mandatory rules:-

> " . . . arbitrators can take into account, as elements of fact, mandatory rules likely to have an impact on the performance of the contract . . . arbitrators may have to decide whether a breach of a law *other than that chosen by the parties to govern their contract*, could have the effect of rendering the purpose of the contract immoral, thus providing grounds on which to hold it void." [30] (emphasis added).

It seems that such considerations could have been applied in the Sandline arbitration. The Sandline Agreement was due to be carried out within the territory of PNG. So, even where English or international law governed the Agreement, the arbitrators could also have considered mandatory rules of PNG law - including the requirements of s200 of the Constitution.

(d) mercenary activity - against international public policy?

In 1989, the UN General Assembly adopted and opened for signature and ratification the *International Convention against Recruitment, Use, Financing and Training of Mercenaries* ("Convention or Mercenaries"). Article 5 of the Convention on

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28 Maniruzzaman, "International Arbitration and Mandatory Public Law Rules in the context of State Contracts: An Overview", *7 Journal Of International Arbitration*, 53, at 54, *et seq.*

29 op cit, at 58.

Mercenaries prohibits State parties from recruiting, using, financing or training mercenaries.

The Convention on Mercenaries requires that it will come into force upon 22 States ratifying or acceding to it. At the time of the *Sandline* Arbitration, this had not occurred. [31]

The UN Commission on Human Rights has been monitoring the activities of mercenary organisations for some time. The Commission, which also had investigated allegations of human rights abuses on Bougainville [32], describes Sandline as an organisation offering the services of mercenaries. [33]

Since adopting the Convention on Mercenaries, the General Assembly has continued to debate the issue of mercenary activity. On 12 December 1997, the General Assembly adopted Resolution number 52/112 [34], in which the use of mercenaries against sovereign States, or against national liberation movements, was strongly condemned as being in breach of the UN Charter.

[The position on what precisely constitutes a "mercenary" and mercenary activity, is not entirely clear, however. There have been calls for conventions and legislation to more effectively proscribe mercenary activities. [35] Article 47 of the 1977 Protocol Additional to the Geneva Conventions of 1949 provides that a mercenary shall not have the right to be either a combatant or prisoner of war; then sets out several cumulative requirements for the definition of "mercenary". These include the fact that the person must have been specially recruited for (and does take part in) an armed

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30 Gaillard and Savage, op cit, at paragraph 1518.

31 By 30 August 2000, some 20 States had ratified.

32 UN Commission on Human Rights, *Report by the Special Reporter on his mission to Papua New Guinea Island of Bougainville from 23 to 28 October 1995*, UN Document E/CN.4/1996/4/Add.2, 27 February 1996.

33 UN Commission on Human Rights, *Report on the question of the use of mercenaries as a means of violating human rights and impeding the exercise of the rights of peoples to self-determination,* UN Document E/CN.4/1998/31, 27 January 1998.

34 United Nations Document A/52/643.

conflict, that the person is motivated essentially by private gain and is not a member of the armed forces of, nor a national or resident of, a party to the conflict. It is suggested that Sandline's personnel would meet these criteria, even though they had been sworn in as "special constables" of the PNG Defence Force. The Protocol applies, however, only to international (ie, between States) armed conflicts. Whilst Bougainville is seeking independence, it remains part of PNG. One could not apply Article 47 to the situation which had developed in PNG].

The international situation forming the background to the *Kuwaiti Airways* case [36] was possibly more "clear cut." The UN Security Council had determined that there was a breach of international peace by Iraq. Iraq's actions were also the subject of almost universal condemnation.

Nonetheless, it was noted in Chapter IV that there is widespread agreement that certain matters offend international public policy - weapons trafficking, drug trafficking, corruption and so on. In this context, and against the background of the formal denunciations of mercenary activity by the UN, it would have been only a small step (arguably, a necessary one) to hold that the Sandline Agreement offended international public policy.

(e) equity and morality

Whilst there may be debate over the sources of international law, it has been noted that one of its sources is equity - "in the sense of fairness, good faith and moral justice." [37] In the text relied on by the Tribunal, *Oppenheim's International Law* [38], it is also noted that equity applies in international law, although not always with a uniform meaning. The authors state that, in general, equity ought to be regarded as a material, but not formal, source of law; however, in a more strictly legal sense, in

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35 *Report of the Special Rapporteur*, UN Doc E/CN.4/1999/11, op cit, at 13.
36 op cit - discussed in Chapter IV.
37 Walker, *Oxford Companion to Law*, op cit, at 639.
38 *Oppenheim's International Law*, Jennings and Watts, eds., Ninth Edition, Longman, 1992.

international law, it can form part of specific rules, or "even part of international law generally." [39] The authors continue that equity can operate on different levels – it can form part of general principle (such as good faith), or a particular rule of law can call for its application, or it could be applied in the sense of Article 38(2) of the Statute of the International Court of Justice, which permits parties to request the Court to decide cases *ex aequo et bono*. [40]

It is clear that, in international law, equity has a significant conscionable element. In this context, it could be argued that it would be against fairness and moral justice to allow a mercenary organisation the benefit from a contract, given that the UN has resolved that mercenary activities violate the UN Charter.

In similar vein, the Sandline Agreement might have been seen as unenforceable because it offended against morality. The authors of *Oppenheim* state that the "rules of morality" ought to apply in public international law "as much as in the intercourse of individuals." [41] The authors note that many principles of international law are underpinned by moral considerations and that:-

> "The progressive development of international law depends as much upon the standard of public morality as upon economic interests. The higher the standard of public morality rises, the more will international law progress." [42]

The authors refer to the rule which provided that immoral obligations could not be the subject of a treaty between States. [43] Uncertainty as to the application of this rule, however, "militated against" its application. Safeguards against possibly immoral

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39 op cit, at 44.
40 ibid.
41 Jennings and Watts, *Oppenheim*, op cit, at 52.
42 ibid.
43 *Oppenhe*im, op cit, at 1216.

treaties now exist in any event due to the "supremacy" of the Charter of the United Nations and the "rules relating to treaties conflicting with *ius cogens*." [44]

The Tribunal's findings

The above discussion is not meant to suggest that the Tribunal should necessarily have reached a different conclusion. There is no doubt that the principles ultimately relied on by the Tribunal are of great import. What is suggested is that there was a wider range of issues for the Tribunal to consider - the Tribunal ought to have looked at other issues, including the public policy considerations of enforcing an agreement for the provision of mercenary services.

Supreme Court of Queensland

By way of aftermath, the matter subsequently came before the Supreme Court of Queensland. [45] PNG indicated that it would seek leave to appeal against the award. Sandline sought security for costs.

Ambrose J, in considering the preliminary issue of security for costs, made some observations on the award itself and the likelihood of success should PNG be granted leave to appeal. His Honour noted that there was some divergence of opinion as to whether the contract was unenforceable under PNG law and whether that rendered the contract unenforceable under English law. [46]

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44 ibid. The expression "*ius cogens*" refers to "peremptory norms of international law" – ibid.

45 *Papua New Guinea v Sandline*, unreported, Supreme Court of Queensland, 22 December 1998, per Ambrose J (Matter Number - QSC 298).

46 op cit, at paragraph 41.

His Honour continued:-

> "It is quite unnecessary and indeed would be quite unhelpful for me to attempt to determine these issues upon an application of this kind. However, having considered all the material which was canvassed had the application for leave to appeal proceeded . . . I have come to the conclusion that there is at least some prospect of Papua New Guinea failing to obtain leave to appeal against the award . . ." [47]

This turned out to be the case. Sandline approached the Court in March 1999, on a preliminary issue, over the construction of s38(2) [48] of the *Commercial Arbitration Act* 1990 (Qld). [49]

The question for consideration was whether an appeal lay under s38(2) on the basis of a question of law arising out of an arbitral award when the relevant determination by the arbitrators involved the application of foreign law. The matter was heard by Ambrose J. His Honour answered the question in the negative. His Honour said that the arbitrators had applied the laws of England, of which public international law formed a part. So far as an Australian court was concerned, this was foreign law. The general rule is that the content of such law is a question of fact to be proved in an Australian court. If the arbitrators made any errors applying English law, these were errors of fact, not of law. [50]

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47 op cit, at paragraph 44.

48 S38(2) provides that " . . . an appeal shall lie to the Supreme Court on any question of law arising out of an award."

49 *Re an Application Pursuant to s38 Thereof by the Independent State of Papua New Guinea v Sandline International Inc*, Supreme Court of Queensland 30 March 1999, Butterworths Unreported Judgments, BC 9901173.

50 op cit, at paragraph 83.

No appeal could lie on a question of fact. His Honour concluded that upon its proper construction, consequently, the term "error of law" in s38(2) is confined to errors of Queensland or Australian law. [51]

[In general terms, the decision leaves something of a gap for parties hoping to set aside or otherwise resist the enforcement of an award. If an arbitration takes place in an Australian State or Territory under the substantive law of another jurisdiction (or perhaps the *lex mercatoria*), firstly, no appeal can lie under the uniform *Commercial Arbitration Acts*; secondly, if the award was then "made" in a State or Territory, a party could not rely on the New York Convention, as, under s3 of the *International Arbitration Act* (Cwth), a "foreign award" is one made in a country other than Australia].

Comments

It is submitted that the *Sandline* arbitration demonstrates a failure by arbitrators to consider and apply appropriate public policy issues. The Sandline Agreement had as its subject matter a purpose which has been condemned by both the General Assembly and Human Rights Commission of the UN. The Tribunal concentrated instead on a few narrow issues - holding that the application of *pacta sunt servanda* was a complete answer. (It is not known if any submissions where made by PNG which touched on the issues referred to above in this Chapter, but the Tribunal certainly did not discuss them on the face of the award).

The highly dubious morality of a State contracting with mercenaries to engage in conflict against its own citizens was seemingly not considered at all. If an activity or course of action, after coming to the attention of international bodies, is deplored or strongly disapproved of in the formal pronouncements of such bodies, then judges and arbitrators have a duty to take cognisance of such matters.

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[51] at paragraph 108.

In *Westacre* (at first instance), Colman J said:-

> " . . . it is relevant to this balancing exercise to take into account the fact that there is mounting international concern about the prevalence of corrupt trading practices." [52]

Colman J confirms that judges must take international concerns into account. His Honour also notes that officials in "certain parts" of the world are "customarily bribed" to procure lucrative contracts. What is also interesting (and relevant) is the way in which His Honour takes note of this particular concern:-

> "Indeed in this very week . . . the government of the United Kingdom together with the governments of many other states is signing the OECD Convention on Combating the Bribery of Foreign Officials in International Transactions. Under that convention the parties are, by art 1, to create a specific criminal offence of bribery of foreign officials . .
>
> It is therefore important that, although the convention has not yet come into force, the English courts should not be seen to be encouraging the corruption of government officials as an instrument of international trade whilst paying lip service to such widespread disapproval." [53]

There are a couple of relevant points here, in the way that His Honour notes what are relevant public policy matters. Firstly, Colman J is prepared to take into account contemporary concerns; secondly, His Honour is prepared to note the activities of an international body (the OECD) and its attitudes towards these serious issues.

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52 *Westacre*, op cit, at 597.
53 ibid.

Surely this goes to the essence of applying public policy - inquiring as to what concerns the community must have priority with over a particular issue, in order to adopt a principled position.

The arbitrators in the Sandline case did not do this. It is submitted that they ought to have done so, even if the issue was not raised. The UN has made a number of pronouncements condemning mercenary activity and note should have been taken of that.

CHAPTER X

GLOBALISATION AND THE CONCENTRATION OF ECONOMIC POWER

> "*Globalisation has something to do with the thesis that we now all live in one world – but in what ways exactly, and is the idea really valid?*" [1]

International commercial arbitration and world trade

International commercial arbitration is an integral part of international trade transactions. Arbitration is:-

> ". . . the preferred method of settling disputes arising out of international commerce." [2]

It is suggested that, because of its very interconnection with international trade, the processes of international commercial arbitration must reflect the values and norms of international trade generally.

This, of course, sets the context for the application of public policy.

The expression which has been used many times to describe what is happening in trade and other international relations is "globalisation." This may not be a new phenomenon. International trade has existed for thousands of years. Perhaps this

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1 Giddens, *Runaway World*, Routledge, 2000, at 25. Giddens answers his own question as to whether "globalisation" is a valid "idea" in the affirmative (at 27). The author notes factors such as the large increase in world trade, as well as the "vast amounts of capital" that are moved around the world "at the click of a mouse", to conclude that " . . . globalisation, as we are experiencing it, is in many respects, not only new, but also revolutionary." The revolutionary aspect comes from rapid developments in technology. (at 28 *et seq*).

2 Lew, *Applicable Law in International Commercial Arbitration*, Oceana, 1978, 1.

expression has become more relevant as the pace of change in communications has rapidly increased in recent times.

In any event, it is suggested that to understand what is driving changes in arbitration, one must examine, if only relatively briefly, the phenomenon of "globalisation."

A. Globalisation

The first difficulty that presents itself is - what is meant by this expression? There have been many attempts to set out what "globalisation" represents. Whilst economic issues are at the forefront, it seems that a significant number of other areas are affected. Twining suggests that the expression refers to:-

> " . . . those processes which tend to create and consolidate a unified world economy, a single ecological system, and a complex network of communications that covers the whole globe, even if it does not penetrate to every part of it." [3]

Giddens says that it is a mistake to see the phenomenon of globalisation as solely involving economic issues - it is "political, technological and cultural" as well. [4] Consequently, it may be difficult to provide a comprehensive definition to help to understand what is involved in the processes referred to as "globalisation".

An important distinction can be made, however, between matters which are of *international* concern and those which are of *global* relevance. On one hand, internationalisation is:-

> " . . . a means to enable nation-states to satisfy the *national interest* in areas where they are incapable of doing so on their own." [5] (original emphasis)

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3 Twining, "Globalization and Legal Theory Some Local Implications" (1996) 49 *Current Legal Problems*, 1.

4 Giddens, op cit, at 28.

5 Delbruck, "Globalisation of Law, Politics and Markets - Implications for Domestic Law: A

On the other, globalisation is a process of *denationalisation* – in the sense of:-

> " . . . interlacing peoples and individuals for the sake of the *common good.*" [6] (original emphasis)

As Aman puts it:-

> " . . . complex, dynamic and social processes that take place within an integrated whole without regard to geographical boundaries. Globalisation thus differs from international activities . . ." [7]

It must follow that jurisdictional authority based on geographic entities is diminished:-

> "Globalisation weakens the regulatory grip national governments have over the economic agents subject to their jurisdiction." [8]

Globalisation is, consequently, the antithesis of internationalisation. The latter involves a positive exercise of state power, whereas the former envisages the retreat or abatement of State power. (Although, it might be argued that for there to be a process of denationalisation, an exercise of State power must occur, that being the decision to withdraw – or not to extend – municipal law in certain areas of jurisdiction. (A State having made such a decision could perhaps, "renationalise" in such areas where it has foregone authority, but may find this a difficult proposition for a number of reasons).

The consequence of this is that the logic of the international political economy forces States to create new rules for international transactions, which leads to the relinquishment of their authority over certain areas. [9]

European Perspective", 1 *Indiana Journal of Independent Legal Studies* (1993), 9, at 10-11.

6 ibid.

7 Aman, "Proposals for Reforming the Administrative Procedure Act: Globalisation, Democracy and the Furtherance of a Global Public Interest", 6 *Indiana Journal of Global Legal Studies* (1998) 397, at 404.

8 Waelde, "International Law of Foreign Investment: Towards Regulation by Multilateral Treaties", [1999] *Business Law International*, Issue 1, 50, at 53.

9 Wiener, "The 'Transnational Political Economy': A Framework for Analysis", University of

As Aman also notes:-

> "The State itself is an agent of globalization, furthering certain processes . . . through, for example, policies designed to attract and retain investment. In so doing, however, the State is also . . . transformed by the very processes it seeks to further . . . Sharing responsibilities with private actors . . . often can mean what once was public is now private." [10]

Aman goes on to discuss certain "models" or contexts for globalisation; firstly, from the perspective of individual States, then in relation to the position of the United States; and, at both how denationalisation may result and how domestic law may be transformed, by the processes under consideration. With regard to "denationalisation", Aman notes that the combination of advanced technology and the extensive deregulation of the flow of capital in world markets, private decisions about economic activity (including production and investment) are being made in the absence of input or control from the State or States affected by such decisions. [11]

Markets are accordingly structured in such ways that State boundaries can become irrelevant. [12] Capital transfers can be made rapidly across boundaries. Transnational corporations acquire finance, carry out research, produce, assemble and market goods in a variety of jurisdictions. In the process, such networks "create relatively integrated markets" and new and complex forms of relationships.

Transnational "players" will accordingly desire that their activities have some form of regulation (if only for their own purposes). As States have retreated, however, there is a regulatory gap:-

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Kent, obtained 7 September 1999, from *speke.ukc.ac.uk*, at 2.

10 Aman, op cit, at 411.

11 Aman, op cit, at 408.

12 ibid.

> "Firms operating internationally need to ensure the functions traditionally exercised by the state in the national realm of the economy such as guaranteeing property rights and contracts." [13]

It is not only a question of seeking order and regulation, but harmonised (or homogenous) regulation :-

> "The principles of private international commercial law, whether they be codified by agencies like the ICC or merely exist in the repeated practices of traders, came about due to the increasing volume and complexity of trade, and the need for simplification, standardisation and predictability." [14]

Certainty (so far as it is possible) is, therefore, important for global commercial activity. This might be achieved in various ways – customs and usage are important, but so too (perhaps more so) are formal regimes and structures, manifested by international institutions and conventions, which must be capable of delivering outcomes within known (and, of course, acceptable) parameters.

Weiner also notes that the "push" for transnational norms creates tensions with territorial sovereignty. [15]

The visible signs of globalisation – international institutions and regimes

Consequently, there are numerous institutions and entities existing at both Government and private level which have as their mission the harmonisation of law.

The charter of UNCITRAL, for instance, is to work toward the "progressive harmonisation and unification" of the law of international trade. On a wider level, UNIDROIT [16] has been established to "examine ways of harmonising and

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13 Sassen, *Globalization and its Discontents*, New Press, 1998, at 97.

14 Weiner, op cit.

15 op cit. The issues affecting developing States which were discussed in Chapter V are one example of these tensions.

16 UNIDROIT, an "independent governmental organisation", is based in Rome. It was initially set up as an auxiliary of the League of Nations and following that body's demise, re-established

coordinating the private law of States and groups of States and to prepare gradually for the adoption by States of uniform rules of private law".

Whilst these institutions *promote* the universalisation of law in various ways, there is an organisation which is actively *creating and enforcing* a body of international law.

That organisation is the WTO.

The WTO

The WTO emerged in 1994 as the institutional successor (in practical, if not in strictly legal terms) to the GATT, following the Uruguay Round of trade negotiations. The GATT itself had come into existence in 1947, following the Bretton Woods Conference in 1944, at which the charters of the IMF and the International Bank for Reconstruction and Development (World Bank) were drafted. These, of course, dealt with financial matters; it was seen that an international regime dealing with trade was also necessary. [17] In 1945, a charter for a proposed International Trade Organisation ("ITO") was drafted, following an ECOSOC resolution calling for a conference on trade.

The GATT was drafted at a conferences in Geneva in 1947. GATT did not possess any legal personality; it was not an organisation *per se*. The intention was that, as an agreement, it would form part of the framework of the ITO; the ITO [18], however never came into existence, due to the failure of the United States to participate. [19]

It has been said that, whilst the GATT was not in the formal sense a legal body, an organisational apparatus nonetheless developed to fill the void caused by the non-

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on the basis of the UNIDROIT Statute.

17 Weaver and Abellard, *The Functioning of the GATT System* [part of a series, *The GATT Uruguay Round: A Negotiating History* (1986-1992), Stewart (ed)], Kluwer, 1993, at 2-3.

18 Watson, Flynn and Conwell, *Completing the World Trading System Proposals for a Millennium Round*, Kluwer, 1999, at 13-14.

19 Weaver and Abellard, op cit, at 5.

materialisation of the ITO. The GATT consequently "evolved to resemble an international organization". [20]

Under GATT, Contracting Parties' obligations were contractual – there was no organisational structure empowered above them with power to make orders. States voluntarily abided by GATT rules and disciplines. [21] Decisions were taken as a result of joint (usually unanimous) action by the members. [22]

Because the GATT did not have legal personality, however, it was perceived, despite its successes, as having shortcomings which could only be resolved by the coming into being of "a new institutional structure". [23] The Uruguay Round of trade negotiations commenced in 1986 and concluded with the signing of the *Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations* on April 15, 1994. Also signed at that time was the Agreement Establishing the World Trade Organisation, with the WTO assuming responsibility for administering the GATT.

The coming into being of the WTO:-

> ". . . . represents a major structural change in the multilateral trade regime." [24]

The principal structural difference is that the WTO is a legal body. Under Article VIII of the Agreement Establishing the World Trade Organization, Members are to accord the WTO such legal capacity and grant such privileges and immunities as are necessary for the performance of its functions.

(Another significant development, of course, was the extension of the regime to cover services and intellectual property rights). [25]

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20 Weaver and Abellard, op cit, at 7.

21 Watson, Flynn and Conwell, op cit, at 37.

22 Evans, *Law-Making Under the Trade Constitution A Study in Legislating by the World Trade Organisation*, Studies in Transnational Economic Law, Volume 14, Kluwer Law International, 2000, at 31.

23 Jackson, *The Jurisprudence of the GATT and the WTO*, Cambridge University Press, 2000, at 455.

24 Watson, Flynn and Conwell, op cit, at 23.

The "Contracting Parties" under GATT are now "Members" of the WTO. Members are required to implement Multilateral Trade Agreements (Article XIV.2) and to ensure the conformity of their laws with their obligations under the Multilateral Trade Agreements (Article XVI.4).

Reich tracks the juridical development of the WTO from the "diplomatic" model of the GATT and argues that the principal driving force behind the progression to a more structured and legalistic regime is globalisation - the greater economic interdependence of States requires that order and certainty underpin international trade relations:-

> " . . . supreme importance is attached to establishing a strong and broadly based world trade regime which will ensure coordination of policies and cooperation on the basis of stability and certainty." [26]

In this context, the WTO has been described as establishing an international "trade constitution", having:-

> " . . . capacity to provide a legal framework for the universalisation of binding norms of substantive law." [27]

There is in existence, accordingly, a powerful institutional framework, with significant lawmaking and coercive powers:-

> "As India recently found out in its patent dispute with the United States, the new trade court has jurisdiction to rule that governments must amend or repeal

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25 Under 'TRIPS' - *Trade Related Aspects of Intellectual Property Rights*, Annexure 1C to Agreement Establishing the World Trade Organisation.

26 Reich, "From Diplomacy to Law: The Juridicization of International Trade Relations", 17 *Journal of International Law and Business* (Winter 1996/Spring 1997), 775 at 839.

27 Evans, op cit, at 4. Evans notes (at 24) that the expression "trade constitution" to describe the framework of the WTO was first coined by Jackson - see Jackson, *The Jurisprudence of the GATT and the WTO*, op cit, at 55. The expression "constitution" in connection with the WTO is also used by Petersmann, "The WTO Constitution and Human Rights", *Journal of International Economic Law*, Volume 3, Number 1, March 2000.

> domestic laws that are inconsistent with world trade norms or risk the imposition of trade sanctions." [28]

The organisation of the WTO comprises *inter alia* the Ministerial Conference and the General Council (both comprised of representatives of all the Members - Articles IV.1 and IV.2). The former is the highest authority within the WTO; it meets at least once every two years and carries out the functions of the WTO (usually via delegation). The latter has responsibility for the day to day operations of the WTO (between meetings of the Ministerial Council) and meets "as appropriate". It operates in "three guises" - firstly, as the General Council and also, as both of the Dispute Settlement Body ("DSB") and the Trade Policy Review Body. [29]

Disputes are heard in accordance with the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"). Article 3.2 of the DSU states that:-

> "The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system."

Parties are encouraged to conciliate and mediate, but if a dispute escalates, the DSB may refer a dispute to a Panel, which is to be comprised of "well qualified individuals". [30]

The Panel must publish a report containing its findings and conclusions, following the hearing of the dispute. Within 60 days of the report being circulated to Members, the DSB is to adopt the report, unless one of the parties chooses to appeal to the Standing Appellate Body. The Standing Appellate Body is established by the DSB and comprises persons of "recognised authority", with expertise in law, trade and the subject matter of the dispute. [31]

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28 Evans, op cit, at 47.
29 This information obtained at the WTO website, www.wto.org, on 19 January 2001.
30 Articles 6, 7 and 8 of the DSU.
31 Article 17 of the DSU.

Reports of the Appellate Body must be adopted by the DSB within 30 days of circulation, unless the DSB decides by consensus not to adopt a report.

Articles 21 and 22 of the DSU provide *inter alia* that there must be prompt compliance with all recommendations or rulings, under threat of the possible payment of compensation, or the withdrawal of trade concessions. The DSB monitors the implementation of recommendations or rulings. The period of time for the implementation of recommendations or rulings can be set by the Member concerned (with the concurrence of the DSB), or by mutual agreement between the parties. If the parties cannot agree, then the matter goes to arbitration and the relevant period may be set under binding arbitration.

Article 25 provides that parties may also refer their initial dispute to arbitration. Articles 21 and 22 DSU apply *mutatis mutandis* to arbitral awards.

Decisions, whether made under the dispute procedures noted, or under arbitration, are consequently binding under the threat of sanctions.

The WTO and trade liberalisation

The powers that the WTO has within its framework are not applied neutrally or disinterestedly. The trade norms established by the WTO reflect the desire for trade liberalisation. The WTO is essentially (as was the GATT) a forum where the interests of producers dominate. [32] To this end, the Most-Favoured-Nation clauses in the GATT (particularly in Article I) promote non-discriminatory processes in trade.

The WTO consequently has at its core a free trade agenda, the rules and norms relating to which are able to be rigorously enforced. This has its origins in classic economic theory:-

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[32] Abbott, "Distributed Governance at the WTO-WIPO: An Evolving Model for Open-Architecture Integrated Governance", *Journal of International Economic Law*, Volume 3, Number 1, March 2000, at 63.

> "The classic economic case for trade liberalization is clear: improved efficiency in resource utilisation. That case holds as much now as in David Ricardo's day and remains at the heart of the rational for an *open trading system.*" [33] (emphasis added).

B. "Judicial globalisation"

Courts are responding to the realities of global trade. Slaughter suggests that courts will pay greater attention to "WTO law", as WTO panels decide disputes. [34] Slaughter also suggests that there is a "judicial globalisation" occurring. This is because the global economy creates "increasingly global" litigation, which is leading to the situation where judges will move from viewing one another as operating in equal but distinct spheres, to:-

> " . . . the presumption of an integrated global legal system. This presumption, in turn rests on a conception of a single global economy in which borders are increasingly irrelevant and an accompanying legal system in which litigants can choose among multiple fora to resolve a dispute, but each of those fora has an equal interest in seeing the dispute resolved." [35]

Globalisation is consequently moulding the way in which courts approach international disputes.

C. The convergence of economic power

Trade liberalisation does not necessarily mean that all States benefit or compete on an equal basis. Weisbrot notes:-

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33 Bergsten, "The United States' Interest in New Global Trade Negotiations", in Schott (ed), *The WTO after Seattle*, Institute for International Economics, 2000, at 44. It seems that Bergsten is alluding to Ricardo's theory of comparative advantage in international trade. For an analysis of Ricardo's work on comparative advantage, see Henderson and Davis, *The Life and Economics of David Ricardo*, Kluwer, 1997, at 457 et seq.

34 Slaughter, "40th Anniversary Perspective: Judicial Globalization", 40 *Virginia Journal of International Law*, Summer 2000, 1103, at 1124.

35 Slaughter, op cit, at 1115.

> "The 'cumulative causation' of unfettered markets - that is, their tendency to concentrate economic development in particular regions at the expense of others . . . " [36]

If it is predictable that the freeing up of markets leads to greater concentration of economic power, then it would seem those with the greatest economic power would be at a relative advantage compared with others. The obvious answer to the question - "where might such power be concentrated at present?" - is the United States.

Reference was made earlier to the threat posed to national jurisdictions by globalisation. This is not true for all States:-

> " . . . the fact remains that the American State has not withered away in the new free market utopia. On the contrary, US hegemony and sovereignty have strengthened in spectacular fashion." [37]

The reasons for this primarily relate to the comparative economic advantage held by the United States in a number of areas. Not only does the United States hold economic advantages, it is the "sole superpower", with a dominant economic, cultural and military position. [38]

In this context, Allott refers to the "heavy responsibility" that the United States has - an imperial responsibility, one which is based on the "sheer facts of American military and economic and cultural power . . ." [39]

There has been some cautionary judicial comment regarding the exercise of United States economic power by the United States Supreme Court:-

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36 Weisbrot, *Globalization for Whom?* Centre for Economic and Policy Research, www.cepr.net. A version of this paper (minus this particular quotation) also appears in *Cornell International Law Journal*, 1998 Symposium Issue, op cit, at 635.

37 Burgi and Golub, "The States We Are Still In", *Le Monde diplomatique*, April 2000 (English Internet Edition, www.mondediplo.com/fr/2000/04/07golub?var_s=burgi+golub).

38 Giddens, op cit, at 33.

39 Allott, op cit.

> "We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws and resolved in our courts." [40]

Such hopes may not accord with reality, however. Aman continues that approaches to commercial law which are designed to effect "uniformity into transnational contractual arrangements" are often seen as being "largely American in nature". [41]

United States investors, in seeking legal security for their investments, desire to "export" their legal values along with their capital. They also seek the liberalising and deregulation of economies (which creates a vacuum into which new rules must go). The United States also requires companies doing business in the United States, to conform to its legal requirements and standards. [42]

In short:-

> " . . . it is the US which is laying down the new groundrules, ie, the dominant economic norms . . . the regulatory criteria and the legal rules (international commercial arbitration)."[43]

Commentators in the United States are urging for even greater reform of international trade, as it is perceived that this is to the advantage of the United States:-

> "The United States has compelling economic, foreign policy and systemic interests in a new round of multilateral liberalizing and rule-making negotiations in the World Trade Organization." [44]

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40 Burger J (for the majority) in *The Bremen v Zapata Off-Shore Co.*, 407 US 1 (1972), at 9.
41 Aman, op cit, at 406.
42 Aman, op cit, at 407.
43 Burgi and Golub, "The States in Which We Still Live", op cit.
44 Bergsten, op cit, 43.

Not only this, but opposition to United States interests must be addressed:-

> " . . . many of the major countries have ideas about the agenda for a new round that are quite different from those of the United States. These differences must . . . be overcome." [45]

In consequence, as the trade regime becomes more liberal (and, as noted in this Chapter, this is the underlying objective of the WTO) the United States and other powerful trade nations will succeed in exporting not only their goods and services, but their approach to regulation as well.

As that happens, authorities such as *Parsons & Whittemore* may become the norm in more and more jurisdictions.

Further, cases like *Parsons & Whittemore* and *Libyan Sun Oil* where United States companies lost their arguments based on political and foreign policy considerations, should not, it is suggested, merely be seen as ideal results of the application of a "level playing field". The regime of *prima facie* equality serves essentially one purpose:-

> "The American doctrine has always been that trade should be open and fair. If everyone is treated equally in the law of international trade, the American belief is that, axiomatically, America will win." [46]

It is the United States which stands to benefit most from the narrow application of public policy.

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45 ibid.

46 Pengilly, "United States Trade and Antitrust Laws: A Study in International Legal Imperialism From Sherman to Helms Burton", 6 (1998) *Competition and Consumer Law Journal* 187, at 188.

Wider significance of *Parsons & Whittemore*

It is in this context that the decision in *Parsons & Whittemore* assumes a wider significance. The case is an attempt by United States Courts *to set an international norm* for the application of public policy.

The reading down of public policy is justified ostensibly as promoting the benefits of international trade *for all participants* by "smoothing the way" for the enforcement of awards in Convention States. This so-called "objectivity", however, masks the reality that the fewer "impediments" there are to international commercial dealings, the more this serves the interests of the United States.

CHAPTER XI

GLOBALISATION AND INTERNATIONAL COMMERCIAL ARBITRATION

> "*Globalization and the impracticability of traditional justice are the forces driving the law of arbitration.*"[1]

Arbitration mirrors the values and norms of international trade

As noted in Chapter X, international trade now operates under an increasingly homogenised global regime. As an essential part of international trade, international commercial arbitration reflects this same phenomenon. Not only is arbitration becoming more "homogenised", but this is happening for specific ends.

In a study of dispute resolution under the NAFTA [2] and MERCOSUR [3] regimes, it was concluded that formal dispute resolution processes inevitably respond to and reflect the particular economic goals being sought under specific trade arrangements. [4]

This phenomenon may apply in a wider context. It is suggested that it is certainly possible (and indeed probable) that dispute resolution processes in general would naturally reflect the general ethos and goals of the international trading community.

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1 Carbonneau, "National Law and the Judicialization of Arbitration: Manifest Destiny, Manifest Disregard, or Manifest Error" in *International Arbitration in the 21st Century: Towards "Judicialization" and Uniformity*? Lillich and Brower (Eds), Transnational Publishers, 1993.

2 North American Free Trade Agreement (entered into between the United States, Canada and Mexico in 1994.

3 Customs union between Argentina and Brazil, coming into force in 1987.

4 Taylor, "Dispute Resolution as a Catalyst for Economic Integration and an Agent for Deepening Integration", 17 *Journal of International Law and Business* (Winter 1996/Spring 1997), 850 at 851.

This desire for order and certainty, so far as it affects the New York Convention, manifests itself in a number of ways.

First, a "harmonious" judicial approach toward the interpretation of the New York Convention is encouraged:-

> "The significance of the New York Convention . . . makes it even more important that the Convention is interpreted uniformly by the Courts." [5]

Second, arbitral processes are becoming less "national", by the "delocalising" both of procedures and awards. Aman states that "perhaps the primary example" of denationalised law is international commercial arbitration proceedings. [6]

The United States' courts approach to the application of public policy to the recognition and enforcement of awards must be seen in this context. Certainty in transactions is regarded as essential to the functioning of international trade. [7] The narrowing of the application of public policy to virtually extreme circumstances obviously leads to much greater certainty in the enforcement of awards.

Some of the "globalising" issues in commercial arbitration will now be discussed.

"Delocalising" or "Internationalising" arbitration

Where general principles of law (as opposed to local or municipal laws) are applied in disputes, arbitrations and awards become "a-national". There are in fact a number of expressions utilised to describe such processes - such as "stateless", "a-national", "trans-national", "de-nationalised" and so on. Firstly, however, a distinction must be made. There is, of course, a difference between the arbitral law (ie, that which governs the arbitral processes) and the substantive law to be applied to the dispute. Either or both of these can be detached from municipal laws.

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5 van den Berg, op cit, at 1.
6 op cit, at 409.
7 See quote from Reich in Chapter X (n.25.)

Procedural law

Van den Berg and Paulsson both state that "a-national" awards come about as a result of the detachment of the arbitral processes from municipal law which governs arbitral procedure. It has also been said that the essence of delocalisation theory is that arbitration may be conducted independently of the law of the place of arbitration, provided that certain minimum internationally recognised standards are observed. The party relying on the effectiveness of an award will not look to the *lex loci* of where it was rendered. [8]

This has two facets - the delocalisation of, firstly, the law governing the proceedings; and secondly, the law governing the award. [9] (Of course, further "international" elements may be involved - the law governing the contract between the parties, and the arbitration agreement itself, could be subject to "general principles of law").

Paulsson says that parties have the power to ensure that delocalised awards result from arbitral proceedings, by providing in their agreements that the law "giving binding effect to the proceedings" [10] is a law other than that of the place of arbitration. According to Mann, however, it is not possible to separate private arbitral processes from the law of the place of arbitration:-

> " . . . every arbitration is necessarily subject to the law of a given State. No private person has the power to act on any level other than that of municipal law . . . The *lex arbitri* cannot be the law of any country other than that of the arbitral tribunal's seat . . .

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8 Chukwumerije, *Choice of Law in International Commercial Arbitration*, Quorum Books, 1994 at 89.

9 ibid.

10 Paulsson, "Arbitration Unbound: An Award Detached from the Law of its Country of Origin", *The International and Comparative Law Quarterly*, Volume 30, 1981, 358, at 360.

> Whatever the intentions of the parties may be, the legislative and judicial authorities of the seat control the tribunal's existence, composition and activities . . . " [11]

The only concession Mann makes to this view is where the parties have expressly agreed that the *lex fori* is to be a law of a State other than that of the arbitral seat. The author then states that, in any event, such a view would not be universally accepted and is not in accordance with what the law should be. [12] Other commentators support this view - eg, Smit, who states:-

> "Arbitration cannot exist outside of a legal context. Institutional rules, such as those of the [ICC] . . . cannot provide the necessary legal basis . . ." [13]

The author continues to the effect that a-national arbitration neither exists nor is needed; all that is necessary is for the "properly applicable law" (which may be a "foreign law") to be determined, to then see if such law will recognise and permit the enforcement of an award. [14]

In England, the view has been taken that it is not possible to "delocalise" arbitration - it is not possible to have arbitral procedures " . . . floating in the transnational firmament." [15] This approach is noted with approval by Redfern and Hunter. [16]

In New South Wales, Giles J has held that it is possible for parties to apply a *lex arbitri* different from the law of the country in which the arbitration is held, but that they cannot escape local mandatory rules. [17]

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11 Mann, "Lex Facit Arbitrum", in *International Arbitration Liber Amicorum for Martin Domke*, Martinus Nijhoff, 1967, at 160-161.
12 ibid.
13 Smit, "A-national Arbitration", 63 *Tulane Law Review* (1988-89), 629, at 631.
14 ibid.
15 *Bank Mellat v Hellinki Techniki SA* [1984] QB 291, per Kerr LJ (CA).
16 op cit, at 90.
17 *American Diagnostica Inc v Gradipore Ltd* (1998) 44 NSWLR 312.

In response to Smit and Mann, it could be said that arbitration takes place because the parties have (exceptions obviously occur in circumstances of compulsion) agreed to that effect. As arbitration usually has a contractual base, it could be argued that the parties may need no further "authority" than contractual capacity and (in the absence of a law expressing a prohibition) freedom to so bargain. Further, if the parties (as they must) impliedly (or expressly) agree to observe any award which follows a submission to arbitration, then should not the parties be able to control the processes by which such an award might come about? The primary concern would be to ensure that such processes must be fair to both sides.

Paulsson (in referring to Lalive) says that to require parties to fit into the vagaries of individual legal systems is akin to Procrustes' demanding of unsuspecting travellers that they fit his bed:-

> " . . . when a party operates internationally, it may have greater or lesser rights with respect to the same relationship or dispute, depending upon the national system which is brought to bear on its case . . ." [18]

Paulsson refers to the *Gőtaverken* case [19] in which the parties chose arbitration in Paris, under ICC Rules. The parties agreed that where the rules were silent, the arbitrators were to decide on applicable provisions. AB Gőtaverken was favoured with the award, which it sought to enforce in Sweden. The Swedish Court of Appeal granted an order of attachment against certain vessels (the same ships which had been built by AB Gőtaverken for GMTC).

In Paris, GMTC commenced two proceedings - the first, an application seeking orders restraining enforcement and the other, an application to have the award

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18 op cit, at 363.

19 *General National Maritime Company (GMTC) v AB Gőtaverken*, noted in *Yearbook Commercial Arbitration* VI (1981), at 221.

declared null and void. [20] The second application went before the *Cour D'Appel*, Paris. The Court noted the parties choice of procedural law and said:-

> " . . . Considering that the arbitral award in question is rendered following a procedure other than that of French law and which is not connected in whatever manner with the French legal system since both parties are foreign and that the contract has been concluded and was to be performed abroad, the award can therefore not be considered as French." [21]

The Court said further that the choice of the place of arbitration was to ensure geographical neutrality. As far as the Court was concerned, the choice of locale was of no importance and "could not be considered as an expression of the implied will of the parties to submit themselves to French procedural law." [22]

The Court accordingly dismissed the appeal, as it had no jurisdiction to hear it. Paulsson states that the importance of the decision lies not so much for its acceptance of the parties right to agree on applicable procedural rules, but for the fact that the decision goes squarely against the idea that the legal system of the arbitral seat has imperative authority to determine whether the proceedings were validly held and whether the award is consequently effective.

The ramifications of a stateless award are significant. As Paulsson further observes:-

> "If detachment of the transitional arbitral process were denied, the choice of the place of arbitration has great significance . . .

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20 Under French law, such separate actions may be maintained - see *Yearbook Commercial Arbitration* VI (1981), at 221, n.1.

21 Extracted from *Yearbook Commercial Arbitration* VI, at 223.

22 op cit, at 224.

> On the other hand, if detachment were accepted, the choice of the place of arbitration is of marginal importance; the award . . . would be cast adrift, its effects to be controlled by no other authority than its (unvarying) contractual foundation and the (varying) requirements of the particular jurisdictions in which it may be sought to be relied on." [23]

In other words, the important question in relation to an a-national award is not what is its status under the law of the seat of arbitration, but rather, can it be enforced in a particular jurisdiction?

The next question might be - what safeguards exist in that jurisdiction to ensure that enforcement is not unfair? Part of the answer might be that if that jurisdiction has adopted the Convention, then there are certain safeguards which are well known and understood, even if not always uniformly applied. Can a party be certain, however, that where an arbitration has taken place without the arbitrators applying a *lex loci arbitri*, that the award can then be enforced under the Convention?

Van den Berg suggests not, in that the Convention applies to the enforcement of awards made in "another State." [24] The proponents of a-national awards, however:-

> " . . . deny that such awards are made in any particular country . . . How can such award then fit into the Convention's scope?" [25]

In any event, the author continues, the "true question" for this issue is:-

> " . . . whether the Convention *requires* for its field of application that the award be governed by a national arbitration law." [26] (original emphasis).

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23 Paulsson, op cit.
24 op cit, at 37.
25 ibid.

Van den Berg believes that the Convention does so require, this being implicit in Articles I and V. The author states that the Convention must be governed by the presumption that awards are governed by municipal arbitration laws, as [referring to Article V.I(e)] jurisdiction for the setting aside of awards remains with the Courts "under whose arbitration laws" the award is made. [27]

There are a number of points which might be made about van den Berg's views. Firstly, with respect, it is probably incorrect to assert that all proponents of a-national awards deny that an award can be "made" in a particular country. Paulsson, shortly after the publication of his article on a-national awards [28], responded to commentary on his views. [29] He noted that what was involved with an a-national award was that it was "independent of "the legal order of its "country of origin." [30]

The a-national award is consequently "made" in a place – but it is not dependent on, nor does it spring from, the law of that place. As the *Cour D'Appel* noted in the *Gőtaverken* case, choice of the situs may have little or nothing to do with choice of law – it may have been made for reasons of geographic neutrality, or for other considerations.

Further, as Chukwumerije states, Article V.I(a) of the Convention reflects the primacy accorded to the will of the parties to choose the applicable arbitration law. [31]

With respect to van den Berg, the wording of Article V.I(e) does not support the conclusion that all awards must necessarily be governed by municipal law. The references to another country in Article V.I(e) are twofold – firstly, to the country "in

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26 ibid.
27 ibid.
28 refer n. 8 above.
29 Paulsson "Delocalisation of International Commercial Arbitration: When and Why it Matters" 32 *International and Comparative Law Quarterly* (January 1983), at 53.
30 op cit, at 57.
31 op cit, at 95.

which" the award is made; and, alternatively, to the country "under the law of which" the award is made. There is a distinction between making an award *in* a country and making an award *under the laws of* a country. Further, with the first of these alternatives, there is nothing which requires that an award made *in* a country must necessarily have been made under the laws of that country, (or indeed any country – it could have made under the procedure set down by, eg, an arbitral institution). The second alternative envisages an award made under municipal law; but the fact of the first alternative must mean that it cannot be the case that all awards must fall under some municipal law.

As, it is submitted, the Convention does not contain the implicit requirement envisaged by van den Berg, an award not made under a municipal *lex arbitri* may be enforced under the Convention (provided, of course, all other requirements are met).

Substantive law

Toope suggests that where arbitrators are authorised (at the instance of the parties) to proceed as *amiable compositeurs*, this results in awards based on a form of delocalised substantive law. [32] This is because, the author suggests, that arbitrators acting as *amiable compositeurs* do not apply any system of law at all. Toope equates arbitrators acting as *amiable compositeurs* with proceedings *ex aequo et bono*, where arbitrators:-

> ". . . simply decide the issues based upon their notions of fairness. This approach is entirely distinct from the operation of 'equity' as a moderating influence within a system of legal rules. In arbitration ex aequo et bono, no legal system is relevant, not even the principles contained in the contract itself, if those principles are deemed to produce an inequitable result." [33]

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32 Toope, op cit, at 22 and 23.
33 op cit, at 63.

Sohn also suggests that *ex aequo et bono* is indeed "absolute equity". An arbitrator, in applying "absolute equity":-

> " . . . may thus disregard existing law and vested rights; he can change a legal situation or refuse to recognise a legal claim to change a situation". [34]

This is not a generally accepted view, however. In the sphere of public international law, for instance, it has been suggested that decisions should be grounded on broad principles. In the *Norwegian Shipowners Case* the arbitral Tribunal were empowered to settle according to "law and equity". The Tribunal said that this expression meant something wider than the traditional Anglo-Saxon meaning:-

> "The majority of international lawyers seem to agree that these words are to be understood as to mean general principles of justice as distinguished from any particular system of jurisprudence or the municipal law of any state." [35]

English Courts have recognised what they describe as "equity clauses" in arbitration agreements. In 1888, the Privy Council heard an appeal from the Court of Queen's Bench for Lower Canada, *Rolland v Cassidy*. [36] Under the Canadian Code of Civil Procedure, arbitrators were permitted to act as *amiable compositeurs*. The Earl of Selbourne said that the Court would "hesitate much" before it could agree that *amiable compositeurs* could disregard "all law" and be arbitrary in their proceedings; the best meaning their Lordships could put on it was that arbitrators so acting may:-

> " . . . dispense with the strict observance of those rules of law the non-observance of which, as applied to awards, results in no more than in irregularity." [37]

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34 Sohn, "Arbitration of International Disputes Ex Aequo et Bono", in *International Arbitration Liber Amicorum for Martin Domke*, Sanders, (ed), Marinus Nijhoff, 1967, at 333.

35 *Norway and United States (Requisition of Shipbuilding Contracts Case),* Annual Digest of Public International Law Cases, Volume I (1919-1922), at 370.

36 (1888) 13 App Cas 770.

37 *Rolland v Cassidy*, op cit, at 772 and 773.

In other words, the role was limited to excusing breaches of contract which are either relatively minor, or which are (or should be) excused by the context.

Some time later, in *Czarnikow v Roth, Schmidt & Co* [38], the parties had agreed that arbitration was to take place under the rules of the Refined Sugar Association ("Association"). The rules provided that the parties were not to require the arbitrators to state a case for the courts in relation to any question of law arising out of their dispute. Such issues of law that arose were to be determined by the Council of the Association. (As noted above, arbitrators in England were required, under the various *Arbitration Acts*, to state a case in relation to an award, or any part thereof). In the course of the proceedings, one of the parties requested the arbitrators to state a case, or alternatively, to allow them to apply to the court for an order directing the arbitrators to so proceed. The arbitrators refused and gave their award. The losing party brought an application to set aside the award, on the basis of the arbitrators' misconduct.

Bankes LJ said that the Association rules purported to oust the jurisdiction of the courts. If these were to be upheld, then the Council of the Association:-

> " . . . is entitled to be a law unto itself and free to administer any law, or no law, as it pleases . . . this is against public policy." [39]

This reflected the Privy Council approach in *Rolland v Cassidy*. The Courts could not permit arbitrators to decide as they pleased, choosing any law, or none at all.

Czarnikow was applied in a later case, *Orion Compania Espanola de Seguros v Belfort Mthe Acttschappij voor Algemene Verzekgringeen*, [40] where Megaw J considered an arbitration agreement which provided that the arbitrators could "abstain from following the strict rules of law" and were to settle any dispute under the

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38 [1922] 2 KB 478.
39 at 486.
40 [1962] 2 Lloyd's Rep 257.

contract "according to an equitable rather a strictly legal interpretation of its terms." His Honour said that there could be no valid agreement to arbitrate if the arbitrators were permitted to decide merely on the basis of what was "fair and reasonable". [41]

A change in approach then occurred. In *Eagle Star Insurance Co Ltd v Yuval Insurance Co Ltd* [42], the arbitration clause provided that the arbitrators were not bound "by strict codes of law", but were empowered to decide in accordance with "an equitable rather than strictly legal interpretation" of the contract. Denning MR said of this clause:-

> "It does not oust the jurisdiction of the Courts. It ousts technicalities and strict constructions." [43]

This view accords with the views of Rubino-Sammartano, who equates proceeding *ex aequo et bono* with Roman *aequitas*, or "equity", which, in civil law systems, may be defined as:-

> " . . . the discretionary authority jointly granted by the parties to a court or arbitrator to mitigate the effects of the application of strict law, when the latter would, in the circumstances, produce unjust results." [44]

It also became clear in England that arbitrators might, in applying equity clauses, go further than the Courts in liberally interpreting contractual terms and in taking a more lenient view of certain breaches. In *Home and Overseas Insurance Co Ltd v Mentor Insurance Co (UK) Ltd (in liquidation)* [45], the arbitration clause empowered the arbitrators " . . . to effect the general purpose of this reinsurance in a reasonable manner rather than in accordance with a literal interpretation of the language".

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41 at 264.
42 [1978] 1 Lloyd's Rep 357.
43 at 362.
44 Rubino Sammartano, op cit, at 9.
45 [1990] 1 WLR 153.

Parker LJ in the English Court of Appeal held that the equity clause being considered by the Court of Appeal, warranted arbitrators, where it was appropriate to do so, "departing from literal or ordinary material meaning." [46]

Lloyd and Balcombe LJJ, agreed with Parker LJ, adding that whilst arbitrators could not be a law unto themselves, there was nothing to stop them adopting a "more lenient" view of a term, or a breach, than a court would adopt. [47]

The courts have also recognised that, some latitude exists within the arbitral processes of adopting a system or body of law to a particular dispute.

In *Orion Compania Espanola*, Megaw J (in the English High Court) said that not only could the parties allow the arbitrator to decide on the basis of a nominated foreign system of law, they could also empower the arbitrator to decide under the principles of international law. [48] This was also acknowledged in *Deutsche Schachtbau-und Tiefbohrgesellschaft GmbH v R'AS al-Khaimah National Oil* [49], in the Court of Appeal. The arbitration took place under ICC Rules, the arbitration clause permitting the parties to choose their own system of law, failing which, the arbitrator could choose the law, by whichever conflict rule the arbitrator deemed appropriate. The English Court of Appeal said that there were three issues to consider when the arbitration clause permitted the selection of a system of law other than a system of domestic law:-

i) did the parties intend to create legally enforceable rights and obligations?

ii) is the arbitration agreement legally enforceable?

iii) would enforcement of the award via the Courts offend against public policy?

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46 *Home Insurance, op cit*, at 162.
47 at 164.
48 *Orion Compania Espanola*, op cit, at 264.
49 op cit.

Sir John Donaldson MR said that the law which might be applied did not necessarily have to be a particular system, but could be an amalgam of several systems, being:-

> " . . . a common denominator of principles underlying the laws of various nations governing contractual relations." [50]

Accordingly, if the applicable law is not that of any particular system, it nonetheless must be recognisable or ascertainable from existing transnational rules or principles.

In the United States, Domke says that deciding *ex aequo et bono* and the "institution" of *amiable compositeur* are "related". He continues that, as far as the United States is concerned, the question of the powers of arbitrators so acting:-

> " . . . need not be investigated in further detail because the practice of commercial arbitration in the United States is indeed that the arbitrator has the freedom of determining the disputed questions according to the justice of the case." [51]

It seems that what Domke is saying is that in *all* arbitrations (although, *prima facie*, he is referring to domestic arbitrations) carried out in the United States, the arbitrators have the implied authority to decide *ex aequo et bono*. Domke states that, in proceeding *ex aequo et bono*, an arbitrator does not disregard substantive law, but may disregard "strict and traditional" law, by which Domke means procedural provisions. [52]

The following points might be made regarding Toope's claims for arbitrations proceeding *ex aequo et bono*:-

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50 At 1035.
51 Domke, op cit at 256.
52 op cit, at 255 and 256.

i) in some jurisdictions, such arbitration does involve the application of general principles of fairness, rather than systems of law;

ii) certain jurisdictions (particularly common law countries), however, permit only relatively minor latitude in such arbitrations; and

iii) those jurisdictions which limit the arbitrators as to how they apply the law may still allow a good deal of latitude in the actual *choice* of law. The parties will not be prohibited from resorting to general rules and principles which have transnational application and recognition.

The *lex mercatoria*

Might the same point as Toope makes for arbitration *ex aequo et bono*, be made for an award based on the *lex mercatoria*? Ie, could the application of the *lex mercatoria* result in a delocalised award?

The lex mercatoria has been described as a "third legal order" – neither municipal nor international law, but "a mixture with the characteristics of both." [53]

According to Goldman, the *lex mercatoria* has "twice disappeared from the face of the earth and twice been resuscitated." [54] The author says that the *lex mercatoria* had an "illustrious precursor" in the Roman *ius gentium* [55], which, as noted above, Francesakis describes as Rome's "international custom of commercial law". The *ius gentium* reflected the rules developed by nations to govern their international commercial relationships and operated as a formally autonomous source of law, "proper to the economic relations (*commercium*) between citizens and foreigners." [56]

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53 Maniruzzaman, "The Lex Mercatoria and International Contracts: A Challenge for International Commercial Arbitration?" 14 *American University Law Review* (1999), 657, at 658.

54 ibid.

55 ibid.

56 Goldman, op cit, at 3.

Goldman states that when all inhabitants of the Roman Empire were granted Roman citizenship in 212 AD, this led to the first demise of the *lex mercatoria*. It no longer had a role in commercial relationships - if all were citizens, then there could be no "foreigners". Parts of the *ius gentium* survived, however, by being absorbed into the *ius civile*, the law which had traditionally governed relations between the citizens of Rome to the exclusion of those who were not Roman citizens. [57] Goldman continues by noting that the original principles of the *ius gentium* disappeared, however, when international economic relations disintegrated in the early Middle Ages. [58]

The renaissance of international relations in the 11th Century caused its rebirth. The later subjection of economic relations to State laws between the 17th and 19th Centuries, however, saw its second "hibernation." [59]

Other writers ignore the genesis of the *lex mercatoria* in Roman times. For example, Stoecker says that the *lex mercatoria* had its origins in the relationships between merchants in Western Europe. At a time when nation states were still basically feudal in nature, commercial law did not exist. Merchants, required to be geographically mobile, came to lay down their own rules for the conduct of business. [60] (Stoecker does also note that marine and customs laws for use in international trade had developed from as far back as 300 BC. [61])

Walker [62] states that the *lex mercatoria* evolved in the Middle Ages, out of the desire of the merchants of Western Europe to regulate their commercial relationships. He acknowledges, however, the influence of Roman law in this process. From the thirteenth century, Italian influences were "directly affecting every country in Europe", this being facilitated by the "general reception" of Roman law. [63]

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57 ibid.
58 ibid.
59 *op cit*, at 4.
60 Stoecker, "The Lex Mercatoria: To What Extent Does it Exist?", (1990) 7 *Journal of International Arbitration*, 101, at 102.
61 ibid.
62 Walker, *Oxford Companion to Law*, Clarendon Press, 1980.

Walker also states that:-

> "There was not a single Law Merchant all over Europe but variations between different states and towns." [64]

Perhaps the most "remarkable feature" of the *lex mercatoria* was that it was developed by the international business community itself, not by lawyers. [65] In 1685, a merchant, Gerard Malynes, put together and published certain tracts in relation to the *lex mercatoria*. Malynes stated that the "Law Merchant" may have been as old as any "humane Law" and "more ancient" than any written Law. [66]

The present day revival is again due to the growth of international trade and the development of professional and trade associations which developed standard contracts.

Form and content of the *lex mercatoria*

One view is that the *lex mercatoria* is recognised as an autonomous norm system, made up of the usages of international trade, together with "general principles of law" and arbitral case law. [67] If such rules are not ascertainable, then the arbitrator must choose the rule or solution which appears most "appropriate and equitable." [68] This is supported by Mustill:-

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63 *op cit*, at 726.

64 *ibid.*

65 Schmitthoff, "The Unification of the Law of International Trade", 1968 *Journal of Business Law*, 105, at 106.

66 Malynes, *Lex Mercatoria, or the Ancient Law Merchant*, 1685, reprinted by Professional Books Ltd, Abingdon, 1981.

67 Lando, "The law applicable to the merits of a dispute", in Lew, *Contemporary Problems in International Arbitration*, Martinus Nijhoff, 1987, at 104.

68 Lando, in Lew, op cit, at 110.

> "In the first place, the lex mercatoria is "anational" . . . the rules of the lex mercatoria have a normative value which is independent of any one national legal system. The lex mercatoria constitutes an autonomous legal order." [69]

Mustill goes on to say that although the essence of the *lex mercatoria* is that it is detached from municipal legal systems, nonetheless at least some of its rules:-

> ". . . are to be ascertained by a process of distilling several national laws." [70]

Goldman speaks of "two different conceptions" of the *lex mercatoria*. The wide view (the principal proponent of which, Goldman says, was Schmitthoff) involves taking note of the object of its constituent parts. This encompasses "transnational customary law", as well as laws and conventions, subscribed to by various states, that "relate to international trade". [71] One may then go further, by also including national laws that relate "specifically and exclusively" to international trade, as well as decisions of national courts on the same subject.

Schmitthoff adopted a positivist approach, stating that the modern law of international trade "may be placed on a firm doctrinal foundation", as international conventions become, by choice, part of national law; also, international customs have become so widely accepted that they:-

> " . . . are capable of being formulated as authoritative texts." [72]

Goldman states his preference, however, for the second approach:-

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69 Mustill, "The New Lex Mercatoria: The First 25 Years", (1988) 4 *Arbitration International*, 86, at 88.

70 op cit, at 92.

71 Goldman, *op cit*, at 5.

72 Schmitthoff, op cit, at 110.

> "The criteria for determining the ambit of lex mercatoria that I would follow . . . does not solely reside in the *object* of its constituent elements, but also in its *origin* and its *customary* and thus *spontaneous*, nature." [73] (original emphasis).

Goldman admits that even the "narrow" approach is also not free from controversy. [74] He refers to two potential sources of difficulty - standard contracts devised by international organisations and Codes of Conduct for international commercial practices. The former do not, strictly speaking, originate from custom; and the latter, should they be regarded as part of the *lex mercatoria* only so far as they reflect international custom? [75]

In order to ascertain the ambit of the *lex mercatoria*, accordingly, one must look to the customs which arose in those times and then to the present customs arising from the actual transactions and dealings between merchants engaged in international trade. It is in the dealings of merchants that one finds the specific problems of international trade; accordingly, the customs of trade are:-

> " . . . certainly the essential element of lex mercatoria." [76]

Ideally then, might the *lex mercatoria* be the agent of the harmonisation of the law or principles governing international trade? Goldman, in suggesting that the *lex* might be utilised as a source of positive law, firstly asks:-

> " . . . is lex mercatoria perceived and applied as a body of legal rules within the international community of merchants, or at least - so as not to prejudice the controverted existence of a *legal order* formed by this international

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73 *op cit*, at 6.
74 Goldman, *op cit*, at 6.
75 *op cit*, at 6 and 7.
76 *op cit*, at 11.

> community - within the *homogeneous* milieu of the agents of international trade?" [77] (original emphasis)

Berman and Kaufman note:-

> "The universality of international commercial law is not solely due to the fact that throughout the world persons who participate in export and import activities confront problems. It is also due to the fact that such persons . . . form a transnational community which has had a more or less continuous history for some nine centuries. It is the mercantile community that has . . . generated mercantile law (and) . . . which continues to develop present day mercantile law." [78]

The authors note that the groups referred to have created "autonomous legal orders on a transnational scale", via trade associations and the use of standard contracts. [79]

Further, "normative" custom "becomes assimilated" to behavioural custom and the norms thereby become binding:-

> " . . . the presumed *expectations* of the participants *in the usage* are sufficient to give rise to the obligation to observe it." [80] (emphasis added)

Consequently, it might be seen that the *lex mercatoria* has been fashioned by practice and conduct. Its observance is largely effected by what might be called "peer pressure" – the expectation that everyone concerned will honour their obligations, because of the "psychological sentiment of the binding force of the usage." [81] It is suggested that this is probably the most logical and appropriate approach to locating

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77 Goldman, *op cit*, at 7.

78 Berman and Kaufman, "The Law of International Commercial Transactions (Lex Mercatoria)", *Harvard International Law Journal,* Winter 1978, at 221.

79 op cit, at 228.

80 Berman and Dasser, in Carbonneau (ed), *Lex Mercatoria and Arbitration*, Revised Edition, Kluwer Law International, 1998, at 64 and 65.

and defining the *lex mercatoria* - to look to the rules which have been formulated to govern the relationships and transactions between those parties who engage in mercantile transactions and who apply and develop the *lex*.

Toope looks at the *lex mercatoria* on another level. He is principally concerned with the area of "mixed" (ie, a State on one side and a private commercial entity on the other) arbitrations. Toope states that the *lex mercatoria* can have little application in mixed arbitrations, as States will have different priorities to those envisaged by the proponents of the *lex mercatoria*. Further, the *lex mercatoria* has, he suggests, as its only goals, the stability and expansion of international commerce. [82] States, on the other hand, have higher objectives - including the fundamental (and quite obviously justified) desire to assert sovereignty over indigenous resources. [83]

Toope refers to Reisman, who argues that the high level of abstraction of the *lex mercatoria* only helps to ensure that large corporate interests can "supplant the legitimate policies of territorial communities". [84] Toope continues by saying that some of the proponents of the *lex mercatoria*, in answering criticisms of the *lex*, have suggested a narrowing of its application. This, he says, reveals as unprincipled the arguments in favour of the *lex* as a "world commercial law." The *lex* ends up being nothing more than:-

> " . . an effort to legitimise as 'law' the economic interests of Western corporations." [85]

This might be true of a number of aspects of international trade.

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81 ibid.
82 Toope, op cit, at 94.
83 op cit, at 97. In this context, see the discussion in Chapter V on arbitrability and "developing" States.
84 op cit, at 95.
85 op cit, at 96.

Have arbitrators applied the *lex mercatoria*?

There have been several instances of arbitrators applying what they described as the *lex mercatoria*. Goldman refers to a number of ICC cases where this has happened. In a Belgian arbitration, *Mechema Limited v SA Mines, Minerais et Metaux* [86], the arbitrator found that the agreement left it to the arbitrator to decide what was the law applicable to the arbitration. The arbitrator then decided that the character of the parties' contract excluded the application of both English and Belgian law and held that the dispute should be determined according to the *lex mercatoria*.

In a decision of the Austrian *Oberster Gerichtshof* [87] the Court held that the arbitrators' decision to apply the *lex mercatoria* did not offend against the public policy of Austria.

Is there a link between the *lex mercatoria* and arbitrators proceeding *ex aequo et bono*?

A link between the *lex mercatoria* and proceeding *ex aequo et bono* might be established in jurisdictions which allow a relatively wide latitude to arbitrators so authorised. In an essay on the application of the principles underlying proceedings *ex aequo et bono* in the sphere of Public International Law, Scheuner [88] looks at what legal or other principles a judge or arbitrator might turn to:-

> "The term "*ex aequo et bono*" refers to certain moral and even legal standards, to a higher sphere of justice . . . The judge may refer to the general idea of justice as adapted to the particular circumstances of the case *or he may find guidance in the fundamental values and standards which, even if they have not*

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86 Yearbook Commercial Arbitration VII (1982), at 77 *et seq.*

87 *Norsolor SA v Pabalk Ticaret Ltd*, Yearbook Commercial Arbitration (1984) IX, 159.

88 Scheuner, "Decisions Ex Aequo Et Bono by International Courts and Arbitral Tribunals", in *International Arbitration Liber Amicorum for Martin Domke*, Sanders (ed), Martinus Nijhoff, 1967, at 274.

> *yet risen to the status of legal rules, are accepted by the great majority of nations . . .*" [89] (emphasis added).

At face value, there appears to be similarities in the processes involved with this approach and that of applying the *lex mercatoria*. Whilst an arbitrator hearing a commercial dispute will not (in the usual course of events) go outside the realm of commercial law or trade usages, the arbitrator in applying the *lex mercatoria*, may attempt to ascertain those rules of law or trade usages which are common to at least some of the States in international trade. [90]

Goldman says that an *amiable compositeur* clause could encourage an arbitrator to apply the *lex mercatoria*. He says further that the rules of international commerce generally correspond with equity and therefore, it is not surprising that *amiable compositeurs* resort to the lex mercatoria:-

> " . . . whose directives they may consider to be naturally and generally in conformity with equity." [91]

UNIDROIT and the *lex mercatoria*

In 1994, UNIDROIT [92] published (after nearly 15 years of negotiation and preparation) its Principles of International Commercial Contracts ("Principles"). The primary objects of the Principles are stated in the Preamble; firstly, that the Principles "set forth general rules for international commercial contracts".

It is then provided, *inter alia*, that the Principles shall be applied when parties provide that their contract be governed by them and may be applied when parties have agreed

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89 op cit, at 283.

90 See, eg, Donaldson MR in the English Court of Appeal, in *Deutsche Schachtbau,* op cit (referred to above in this Chapter).

91 Goldman, *op cit*, at 12.

92 The International Centre for the Unification of Private Law, which is an intergovernmental agency based in Rome. Its purpose is to examine ways of harmonising and coordinating the private law systems of States and to provide uniform instruments of private law. Australia is a member, as are the United Kingdom, the United States and Switzerland.

that their contract be governed by "general principles of law, the *lex mercatoria* or the like."

It is also (from the Preamble) intended that the Principles may serve as models for "national and international legislators". The Principles contain provisions relating to:-

- party autonomy, in entering into contracts and choosing the content;
- formation of the contract and its validity;
- interpretation and performance; and
- non-performance and remedies.

The ICC has published a collection of short papers concerning the Principles [93], in which a case is made for regarding the Principles as a "new *lex mercatoria.*" Komarov suggests that in order to deal effectively with an international dispute, this requires:-

> " . . . not only internationalized procedure, but also substantially internationalized substantive rules." [94]

The difficulty with reliance on national legal systems, he continues, is that as they are more bound to the "internal social and political structure" of States, thereby making the application of law to international disputes "unpredictable." [95] Komarov continues that the great advantage of the Principles is that they greatly diminish the principal argument against the parties nominating as their choice of law, eg, "general principles of law" or the *lex mercatoria.* The difficulty in so doing is the "vagueness and uncertainty" that such choice of law brings. Such choice nonetheless indicates that the parties wish that the substantive rules governing their relationship should be free

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93 *The UNIDROIT Principles for International Commercial Contracts: A New Lex Mercatoria?* ICC/Dossier of the Institute of International Business Law and Practice, 1995.

94 Komarov, "Remarks on the Applications of the UNIDROIT Principles of International Commercial Contracts" *in International Commercial Arbitration*, ICC, op cit, at 157.

95 ibid.

of any national system of law. The Principles resolve the "vagueness and uncertainty" that choosing the *lex mercatoria* involves, by their "concrete, if not precise, contents." [96] In other words, the Principles are an identifiable set of rules to which resort may be easily had. The arbitrators do not have to embark on an inquiry to find the *lex mercatoria*.

The *lex mercatoria* and public policy

The suggestion has been made that if the *lex mercatoria* is separate from both municipal and international law, it is consequently divorced from the operation of public policy. [97]

This cannot be the case. Despite differences over its nature and content, the *lex mercatoria* is nonetheless, first and foremost, a *lex*.

As it is international in character, then, in the case of a contract governed by the *lex mercatoria*, the arbitrators can look to international public policy, as well as the public policy of the place of arbitration and the likely place of enforcement. [98]

Comments

International commercial arbitration "reflects" what is happening in international trade because it is an essential part of international trade.

The desire for uniformity is manifested in various ways - the encouraging of a "standard" approach to the interpretation and application of the New York Convention, the use of a-national awards, the application of the *lex mercatoria* (or at

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96 Komarov, op cit, at 160 and 162.
97 Maniruzzaman, op cit, at 704.

least "general principles of law"), the authorising of arbitrators as *amiable compositeurs*, or proceeding *ex aequo et bono*.

All of these factors lead to the greater homogenisation of both procedural and substantive law, which is the desired outcome, at least in a number of Western jurisdictions. The evolution towards greater certainty is mandated, not just for the sake of efficiency *per se*, but by the demands of the actors in international trade.

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[98] op cit, at 705.

CHAPTER XII

RECOMMENDATIONS

> "*This is only one view of international law, but nonetheless it gives an important indication of the relevance of law as an institution for protecting community values.*" [1]

"Pro-arbitration"

The evolution of public policy to a "pro-arbitration" position has certain obvious attractions. Parties to an international contract may have access to a dispute resolution process which is speedier and more flexible (and consequently less expensive) than court-based processes. Moreover, utilising arbitration may place less of strain on a commercial relationship than resorting to court action; and, as some commentators have noted, arbitration may be more "neutral", in that parochial decisions can be avoided.

This evolution, against the background of increasing international trade, has led to a more "hands off" approach by courts in certain (mainly Western) jurisdictions. Public policy is being selectively applied - "pro-arbitration bias" and the desire for finality of awards are being seen as being more important than the upholding of public values and interests and the integrity of public institutions. The outward manifestations of this are the factors discussed in Chapter XI (such as the revitalisation of the *lex mercatoria*), the liberal approach to arbitrability and a

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[1] Blay, Piotrowicz and Tsamenyi, *Public International Law An Australian Perspective*, Oxford University Press, 1997, at 3.

restrictive approach to the application of public policy, particularly in the enforcement of awards.

The New York Convention has been described as having a "pro-enforcement bias." [2] The meaning of this is open to interpretation - but, on one view, it goes without saying that the Convention is "pro-enforcement." The idea of the Convention is to facilitate the enforcement of awards.

What is clearly *not* envisaged by the Convention is the reading down of the public policy defence. The framers of the Convention saw that the "safety valve" of public policy was necessary.

As there is the potential for almost any matter involving commercial or economic issues to be arbitrated and for the resultant award to be enforced with a minimum of intervention, the public interest requires supervision of arbitration, at least to the extent necessary to ensure that the public interest is observed in arbitral processes and the integrity of public institutions is preserved.

Private arbitration requires public supervision

Whilst public policy is, by its very nature, "public", commercial arbitration is a private process. The interpretation of agreements, the application of the law, the investigation of disputes and their resolution is all carried out in private:-

> "At the transnational level, are we seeing the development of a new ius mercatoria – a system of largely private regulation within the capitalist world economy with institutions such as international arbitration playing an increasingly significant role." [3]

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2 *Parsons & Whittemore*, op cit, at 973.

3 Twining, "Globalization and Legal Theory – Some Local Implications", (1996) *49 Current Legal Problems*, 1.

Lew's observation that arbitrators are the private guardians of international commercial transactions [4] assumes much greater significance following the flourishing of commercial arbitration. The very fact that regulation is becoming increasingly privatised calls for greater, rather than less, vigilance in the public interest.

Issues

As was argued in Chapter VII, it follows that authorities such as *Parsons & Whittemore* must be regarded as being wrong in emphasising a restricted role for public policy. There is a clear duty to apply public policy, not to restrict it so that it becomes virtually meaningless.

It is suggested that, in this context, the following issues are relevant:-

- the "internationality" of public policy;
- whether public policy ought to be modelled on common law or civil law considerations;
- its structure;
- its content; and
- whether a court for international commercial arbitration ought to be established.

These issues will now be discussed.

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4 Noted in Chapter IV.

"Internationality" of public policy

As was noted in Chapter IV, a truly international public policy is now recognised. In this era of globalisation, States ought to continue to develop cooperatively a "genuinely international" public policy.

It has been seen that, as the world's trading system becomes more integrated, the rules of private international commercial law have grown and adapted to accommodate this.

International public policy could be fostered in a number of ways. It will be suggested later in this Chapter that a Court for International Commercial Arbitration should be established. One of the duties of such a Court would be to ensure that public policy was developed and observed.

Until such a Court is established, however, municipal courts should continue to develop universal policy positions. As was noted in Chapter X, Slaughter suggests that "judicial globalisation" is occurring, characterised by an increasingly cooperative approach to dispute resolution. This cooperation could extend to a more consistent approach for developing and applying international public policy.

This will not be a simple task. Weiner's comments regarding the tensions between international norms and State sovereignty are particularly apposite. As outlined in Chapter X, the United States' Courts attempt to set an international norm via *Parsons & Whittemore* and the cases which have followed, is designed to serve the interests primarily of the United States, which has elevated itself to being the prime "norm-setter."

This leads to the point as to whose interests must be protected via an international public policy. An international community must be identified as being the community or "public" on whose behalf international public policy is ascertained and applied. One suggestion could be that the "international trading community", ie, those parties mostly utilising international commercial arbitration, could be recognised as the relevant "community".

This may be too narrow, however. Some writers have taken a very "global" view of international interaction:-

> "A completely contextual, configurative theory about law will recognise that today mankind interacts on a global . . . scale. In the sense of interdetermination with respect to all values, the whole of mankind presently constitutes a single community, however primitive." [5]

Practically every nation State will have a vested interest in the maintenance of an effective approach to public policy (whether domestic or otherwise), and would not wish to see faith in their laws and public institutions suffer. As municipal courts have the power to determine whether arbitral awards may be enforced, the "international community" which has the vested interest in maintaining an effective public policy at an international level, must be, it is suggested, all concerned nation States.

The community created at an international level has common interests and values. In the present context, it is suggested that individual States must share the same basic desires as to the efficacy of international public policy - so the community is formed by all interested States on behalf of their citizens.

As Simma and Paulus note, the idea of an international community is still evolving [6] and that, whilst international law is becoming more institutionalised, that idea is still as much "aspiration as reality." [7]

That should not prevent there being identifiable international public interests to protect.

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5 Lasswell and McDougal, "Criteria For a Theory About Law", 44 *Southern California Law Review*, 1970-1971, 362, at 388-389.

6 Simma and Paulus, "The 'International Community': Facing the Challenge of Globalization", *European Journal of International Law*, Volume 9 (1998), Number 2, 266 *et seq.*

7 Simma and Paulus, op cit, at 277.

"Civil law" or "common law " public policy?

It is generally considered that civil law public policy ("*ordre public*") is a broader concept than common law public policy. During the discussions on Article 34 of the UNCITRAL Model Law, it was noted that the former may be said to include principles of procedural justice, whilst the latter excludes such notions. [8]

It was eventually decided that the broader notion was deemed the more appropriate – the Commission Report noting that "public policy" covers procedural matters, as well as "fundamental principles of law and justice". At one stage, the Working Group did consider whether an additional ground of "procedural injustice" might be included in Article 34; this was rejected, as the Working Group decided, in what Holtzmann and Neuhaus describe as a "fundamental policy choice" [9], that conformity with Article 36 (which in turn was to conform with Article V of the New York Convention), was preferable. It was said that it is important to enhance "predictability and expeditiousness". In any event, as had been agreed, public policy could cover procedural problems. [10]

Despite deciding upon harmony with Article 36 and the New York Convention, it was considered at the Working Group's following session whether "manifest injustice" ought to be added as a separate defence. This was rejected, as being "too vague and too broad" and it was again confirmed that, in any event, public policy could cover this area. [11] The Commission Report continued:-

> "It was noted . . . that the wording 'the award is in conflict with the public policy of this State' was not to be interpreted as excluding instances or events relating to the manner in which an award was arrived at." [12]

Public policy would then include (perhaps the more flagrant) breaches of due process, or natural justice.

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8 Holtzmann and Neuhaus, op cit, at 914.
9 Holtzmann and Neuhaus, op cit, at p.912.
10 ibid and p.913.
11 ibid.

Adopting the civil law "model" must consequently lead to a wider body of principle being available than if the common law approach was adopted.

Structure

Bell proposes a number of models that courts might apply in considering public policy issues. It is suggested that two of these may be relevant for present purposes - the "Consensus" Model and the "Rights" Model. [13] The first of these may be utilised where reference may be made to the "fundamental values and purposes" of society; where it is not so much a case of the judge deciding within the limits of an accepted framework of values, but where the "consensus dictates the solution." [14]

This model could indeed apply where the matter under consideration by a court or arbitrator is (practically) universally accepted or notorious.

The second model ("Rights"), which Bell bases on the works of Dworkin, encompasses looking at the individual rights involved with any particular issue. This can be applied from the perspective of a party seeking to enforce alleged rights - such rights may be denied, as:-

> " . . . the plaintiff has failed to make out a strong enough moral claim to what he requests." [15]

This approach is reflected in the laws of many countries, where a plaintiff might be restrained from exercising what are otherwise legal rights. Intervention is justified on the basis that the plaintiff's behaviour is, in the circumstances, against conscience.

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12 Holtzmann and Nuehaus, op cit, at p914.
13 Bell, op cit, at 9 *et seq.*
14 op cit, at 12 and 14.

This has not only been the position at equity, but is now reflected in many statutes and codes.

Applying such considerations to a party seeking the enforcement of an arbitral award, refusal could be justified, if it appeared that the party's claim was unconscionable, or morally indefensible.

As it is suggested that public policy ought to be expanded beyond its present narrow scope, Bell's "Consensus" model is probably inadequate for these purposes. A more expansive approach is needed, and the "Rights" model could assist, without necessarily providing a complete answer.

Content

(a) "existing" public policy

In a paper prepared for the ILA London Conference in 2000, the ILA's Committee on International Commercial Arbitration stated what it believed to be the content of international public policy (so far as the New York Convention was concerned). The Committee firstly noted that the United States in particular took a restrictive view of public policy. This was also the case in England, where the courts have "affirmed the importance of finality of awards." [16]

The Committee noted that recognition of the importance of finality in awards is, of course, itself "an aspect of public policy." [17]

The Committee then identified four sub-categories of substantive "rules and norms":-

- mandatory laws (*lois de police*);

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15 op cit, at 204.

16 International Law Association Committee on International Commercial Arbitration, *Interim Report on Public Policy as a Bar to Enforcement of International Arbitral Awards*, London Conference (2000), at 15, 16.

17 ibid.

- fundamental principles of law;

- public order/good morals; and

- national interests/foreign relations.

The Committee then described these sub-categories. [18] The first refers to imperative provisions of law which must apply to an international relationship even if, because of the operation of conflict provisions, the body of law to which they belong does not govern that relationship. The second sub-category refers to generally shared principles, which include good faith, *pacta sunt servanda*, the prohibition against unconscionable behaviour and the protection of those incapable of acting. The third comprises activities which are contrary to morality, such as drug trafficking, terrorism, genocide and slavery. The Committee also noted that it was arguable that an international consensus existed that corruption and bribery are contrary to international public policy. [19]

The last sub-category covered instances where an award might breach sanctions or boycott legislation. In that context, the Committee noted the warning in *Parsons & Whittemore* that parochial political interests should not operate under the guise of public policy.

It is submitted that the sub-categories identified by the ILA sub-committee are an excellent starting point for debate on the content of public policy. [20]

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18 op cit, at 15, et seq.

19 op cit, at 22.

20 The ILA Committee reconvened at its New Delhi Conference in 2002. It published a number of Recommendations "as to the application of public policy by State courts". The Recommendations *inter alia* affirmed that courts have a limited role in the enforcement process and that public policy should be invoked only in "exceptional circumstances" – Recommendations 1(a) and 1(b). Further, a rather narrow view of what constituted international public policy was adopted – it was not to be understood as referring to public policy which might be common to States (which was described as "transnational" public policy), but as that part of the public policy of a State which would prevent it from invoking a foreign law, judgment or award – Recommendation 1(b). There seems to have been a narrowing of the Committee's views from the 2000 Conference. It is perhaps worth noting that the Committee stated that members from developing countries opposed the idea that courts were only to have a limited role in the enforcement process. (International Law Association

There will probably be little argument over the first two categories, although some comment might be made about unconscionable behaviour.

Whilst many arbitrations are conducted between transnational corporations capable of asserting and maintaining their own rights, there may be occasions when particular parties are unable to do so. For instance, there is an increasing trend in Europe to permit arbitrations in international consumer and employment contracts. [21] Junker cites instances where the German courts use guidance from the German Code of Civil Procedure, adopting the concept of the unfair use of an economically stronger bargaining position. [22]

Obviously, there is potential for unconscionable behaviour where the parties have disparate economic power. This must influence not only the performance of contracts, but the conduct (and, therefore, probably the outcomes) of arbitrations. Many statutes in both common law and civil jurisdictions now include provisions relating to unconscionable behaviour - stronger parties should not take undue advantage of their relative strength. That disparities exist is beyond doubt:-

> "Trade has not caused any country to sink into poverty, but neither has the trading system paid adequate attention to the unequal distribution of its benefits." [23]

As noted in Chapter XI, it has been observed that economic power is being concentrated in the United States. The disparities in economic power ought not to be used to unfair advantage. As Kirry notes, referring to Plaisant and Motulsky:-

> " . . . arbitration assumes the balance of respective strength; where this balance no longer exists, arbitration becomes asphyxiated." [24]

Committee on International Commercial Arbitration *Final Report on Public Policy*, ILA, 2002).

21 Kirry, op cit, at 388 and 389.

22 Junker, op cit, at 247.

23 Abbott, "Distributed Governance at the WTO-WIPO: An Evolving Model for Open-Architecture Integrated Governance", *Journal of International Economic Law*, Volume 3,

It may be the case that courts are becoming more interventionist on the basis of unconscionable behaviour. In *Olex Focas Pty Limited* v *Skodaexport Co Limited* [25], Batt J in the Victorian Supreme Court was prepared to injunct a beneficiary from calling on a bank guarantee, as to have done so in the circumstances would have been unconscionable. The decision represented something of a ground-breaking approach, as the general rule is that beneficiaries may only be restrained from calling upon guarantees if fraud can be established. [26]

With the ILA Committee's third and fourth categories some debate may be necessary, and creativity needed. In the third category, it is submitted that the position on bribery and corruption should move beyond the "arguable" to the definite. International concern over these issues has continued to grow. [27] The social and economic effects of corruption can be so significant that the time has surely come for seeking an international consensus that bribery and corruption are contrary to international public policy.

The third and fourth categories possibly overlap to a certain extent. For instance, during the apartheid era, an agreement which promoted the aims of or was exploitative of apartheid, may have been objectionable not only on the grounds of morality, but also on the basis of boycotts and sanctions agreed by international bodies. In more recent times, such considerations could extend to an agreement which involved large scale corruption, given that the *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* has opened for signature.

It is also suggested that the fourth sub-category could be expanded beyond formal sanctions and boycotts. Reference could be made to eg, the UN Charter, or a

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Number 1, 2000, at 63.

24 ibid.

25 (1997) ATPR (Digest) 46-163.

26 Of course, in relation to fraud, if it can be established that the award itself has been obtained by fraud, then public policy should intervene here also and enforcement refused. *Westacre Investments*, at first instance, op cit, at 607.

27 See the commentary at the beginning of Chapter VIII.

Declaration of the General Assembly, to see if what is being complained about in any arbitration dispute involves a possible breach of the Charter, or a Declaration.

The UN should be a vital source of inspiration for international public policy:-

> "The UN has an important impact on the shaping of common values, be it in the General assembly or in convoking international conferences . . ." [28]

There has been some debate as to the binding nature of the United Nations Charter and Declarations and Resolutions of the General Assembly. [29] It is suggested, however, that it may suffice for public policy considerations if an activity breached the United Nations Charter, or was condemned by a resolution of the General Assembly, as have, for instance, commercial corruption and the hiring of mercenaries.

Of course, other international institutions such as the OECD may also take an interest in a particular matter, and reference could be made to any conventions or formal policies of such organisations.[30] This is what Colman J did in *Westacre*, at first instance.

In this context, it should be noted that courts have for long gone outside of strictly "legal" sources to find answers to difficult problems, and to aid the development of the law. Judges may:-

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28 Simma and Paulus , op cit, at 274.

29 See, eg, the discussion in Schermers and Blokker, *International Institutional Law*, Martinus Nijhoff, 1997, at paragraphs a 1248 et seq; Chowdhury, in Hossain (ed), *Legal Aspects of the New International Economic Order,* Frances Pinter (London) Nicols (New York), 1980 at 82, et seq; and Mendelson, in Hossain, op cit, at 95 et seq.

30 As noted in Chapter VIII, commercial corruption has received considerable attention not only from the United Nations, but from organisations such as the OECD. Of course, the depth of attention accorded a particular matter and the fact that a number of organisations or institutions may have become interested in it, would bear upon any decision to regard the matter as being objectionable on public policy grounds – the greater the attention, the more likely it would be that the matter ought to be so regarded.

> " . . . look to propositions from outside the law, corresponding to supposed *empirical knowledge or accepted values* of the present time and place, and thus relevant to the doing of justice within these." [31] (emphasis added)

Courts are consequently accustomed to looking at societal experience, or widely accepted norms, in resolving legal issues. The application of public policy involves, as Stone has noted, an element of creativity. Resorting to extra-judicial sources is part of this. [32]

(b) an additional category of public policy - manifest injustice?

One further issue raised by the ILA Committee at its 2000 Conference (and which was also raised in the discussions on the UNCITRAL Model Law) [33] is the issue of "manifest injustice". Whilst this was rejected as grounds for a separate defence, it might be argued that a completely perverse or egregious decision ought to be refused enforcement (provided no other defences apply) on public policy grounds.

Some guidance might be provided by the United States where reliance on "manifest disregard of the law" is available in the United States as a basis on which to attack a domestic arbitral award. In *Merill Lynch, Pierce, Fenner and Smith, Inc*, "manifest disregard" was noted as being something beyond mere error - it may occur where the arbitrator correctly states the law, but then does not apply the law. [34]

United States courts, however, have expressly refused to recognise that "manifest disregard of the law" could provide a defence to enforcement under the New York Convention. In *Brandeis Instel v Calabrian Chemicals* the District Court (SDNY) discussed whether the "manifest disregard" was indirectly available to the defendant, as falling under the public policy defence. The Court said that it was not, as only if

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31 Stone, *Precedent and Law*, Butterworths, 1985, at 31.
32 see, generally, Chapter IV.
33 As noted above in this Chapter - refer n.8.

"the most basic notions of morality and justice" were offended, would the public policy defence apply. Manifest disregard:-

> " . . . does not rise to the level of contravening 'public policy' as *that* phrase is used in Article V of the Convention." [35] (original emphasis)

In *Industrial Risk Insurers v MAN Gutehoffnungshütte,* whilst the point was argued, the issue as to whether "manifest disregard of the law" fell under public policy was hardly discussed by the Court of Appeals (Eleventh Circuit), it merely being noted that the defences under the Convention were exclusive. [36]

What might be the effect, however, of including "manifest disregard" as an available defence within supra-national public policy? It is suggested that this is a difficult issue. A party may suffer because of a perverse decision, but have no grounds of redress under the New York Convention. The arbitration may have been conducted on an unchallengeable basis. Yet, the award itself might be totally unjustified. Where does this leave the offended party?

On one hand, it could be suggested that whilst this may be unfortunate, there should be no redress. The parties, having chosen their dispute resolution process, must (in the absence of something akin to fraud) be accepting of the possible outcomes. It might also be argued that including this defence under public policy would greatly widen the ability to oppose an application for enforcement and consequently, the number of matters coming before the courts. Parties may readily allege "manifest disregard" in any decision that goes against them.

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34 op cit, at 937.
35 op cit, at 165.
36 op cit, at 1445–1446.

On the other hand, it was noted during the debates on the UNCITRAL Model Law that this avenue was not precluded. [37] It is suggested that if this ground of defence were to be included under public policy, then the "manifest disregard" or manifest injustice perpetrated in arriving at an award should be immediately apparent – ie, the disregard or error should indeed be readily manifest.

The United States' authorities affirm that, for "manifest disregard" to succeed, the error must be obvious and capable of being readily and instantly perceived by the average person qualified to act as arbitrator. [38] As was noted in Chapter V, court time should not be taken up with extensive preliminary argument. In *Antaios Compania v Salen Rederierna*, Saville QC (later Saville LJ) submitted that there was "disquiet in the city", not over the "Nema" guidelines laid down by the House of Lords, but:-

> " . . . the extensive hearings before a commercial judge whether there should be an appeal from the arbitrator at all." [39]

Consequently, in order to avoid these difficulties, in considering whether manifest injustice ought to form a public policy exception, the error must be one which is readily apparent. The degree of error must also be significant, so as to substantially prejudice the interests of the complaining party.

In a Canadian decision (in the Superior Court of Quebec), *Navigation Sonamar Inc v Algoma Steamships Limited* [40] Gonthier J considered an argument that "manifest disregard" offended against the public policy of Canada. [41] His Honour seemed to accept that this could be the case, even though His Honour did not find "manifest

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37 As noted above – see n.23.
38 *Merill Lynch, etc, v Bobker*, op cit, at p. 933
39 *The "Antaios"*, op cit, at p.197
40 Superior Court Quebec, District of Montreal, Number 500-05-000385-870, April 14, 1987.
41 A public policy defence to a claim for enforcement is available under Article 36 of Canada's *Commercial Arbitration Act* 1985.

error" in the particular award. Gonthier J referred to a text by Pépin and Oullette, in which reference was made to the "notion of error of law on the face of the record":-

> "It is viewed, in some manner, as some kind of insult to the law, a significant error, gross or intolerable in respect of which judges cannot refrain from exercising their power of review." [42]

It is suggested that the criteria referred to by Gonthier J would be appropriate to form a test to establish whether "manifest error" has occurred. Such a test would be in accordance with considerations of the public interest, in that intervention must be justified in the case of a truly perverse award, as its enforcement would greatly detract from the administration of justice.

What follows is that public policy ought *not* to be expanded to include relatively trivial concerns. For instance, where an award is made in a form which might offend relatively minor local procedural requirements.

The recognition of manifest injustice can still accommodate desires for efficiency. If there is insufficient basis on which to challenge an award after a necessarily brief consideration as to whether a manifest error appears, then the award should be enforced as expeditiously as possible.

Summary

- public policy should be modelled on civil law concepts, so as to include examples of manifest injustice (within the parameters described above);

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[42] Pépin and Oullette, *Principes de contentieux administratif* (1979), at 223.

- the sub-categories identified by the ILA should form the basis for the content of international public policy, to which may be added the additional sub-categories discussed;

- public policy should be developed creatively, by the utilisation of various sources;

- the public policy of affirming the finality of awards should also be maintained, with the proviso that, as awards are not like judgments, the policy concerning the finality of awards should not be relied upon to allow fraud, corruption and the like to be ignored.

A Court for International Commercial Arbitration

State power, centred in State institutions is exercised by those appointed to public office:-

> "The judges are the delegates of the Queen . . . they represent her to execute law and justice, in mercy." [43]

The question arises as to how juristic values can function at international level. One way would be to establish an international court. At the Centenary Conference of the LCIA (in 1993), Judges Holtzmann and Schwebel proposed the establishment of an international court for commercial arbitration and suggested that this court (which the present writer will call the Court for International Commercial Arbitration - "CICA") would make orders for enforcement which would automatically be enforced by municipal courts unless public policy was offended. [44]

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[43] Lord Denning, Manitoba Law School Foundation Inaugural Lecture, *Manitoba Law Journal*, Volume 6, Number 1, 1966.

[44] See also Pechota, "The Future of the Law Governing the International Arbitral Process", in

CICA could then be seen as being the equivalent of other supra-national bodies (for instance, the European Court of Human Rights and the recently established International Criminal Court) in upholding legal and moral principles relevant to a particular subject or body of law.

The first European Court of Human Rights was established in 1959. Its object was the enforcement of the *Convention for the Protection of Human Rights and Fundamental Freedoms* (also known as the "European Convention on Human Rights") which had entered into force in 1953.

A series of Protocols have been added to the European Convention on Human Rights which, *inter alia*, provide for individuals to bring claims based on breaches of the European Convention. Protocol 11 established new enforcement procedures, as well as a new European Court of Human Rights, which came into existence on 1 November 1998. The Court sits in Strasbourg and is comprised of the same number of judges as there are Contracting States. Judges, however, do not "represent" any particular State, they sit in an individual capacity. They must not engage in activity likely to prejudice their independence or impartiality.

The International Criminal Court was established by the *Rome Statute of the International Criminal Court*. [45] The Court has international legal personality, and may initiate prosecutions of its own volition. The Statute also provides that judges of the Court must be independent in the performance of their functions, and they may not engage in any activity likely to interfere with their judicial functions or their independence.

Carbonneau, *Lex Mercatoria and Arbitration*, op cit, at 257.

45 The Statute was adopted in Rome on 17 July 1998, at the United Nations Conference on the Establishment of an International Criminal Court. At the same time, the Statute was opened for signature. The Statute was ratified in 2002, and entered into force on 1 July 2002. The United States signed the Statute on 31 December 2000, but advised the Secretary-General on 6 May 2002 that it would not become a party.

Of interest are the provisions in Article 21, which set out the law the Court is to apply. This may include:-

> "(b) . . . principles and rules of international law . . . (*and*)
>
> (c) . . . general principles of law derived by the Court from national laws of legal systems of the world, including as appropriate, the national laws of States . . . provided that those principles are not inconsistent with this Statute and with international law and internationally recognised norms and standards."

It is noted that the Court may have regard to international norms and standards; against which any principle under consideration for possible application may not offend. It is also interesting to note that legal principle may be subjugated to moral considerations in certain circumstances.

Establishment of CICA

The foundation document for CICA could draw inspiration from those already in place for the above-mentioned institutions. Like the European Court for Human Rights, it would exist to enforce a specific convention; like the International Criminal Court, it could draw upon a substantial body of international law, with due regard being paid to "international norms and standards." As with both, the independence of the judges would be guaranteed.

Of course, there are other issues – for instance, how would the CICA be constituted? Perhaps most logically, as an organ of the UN. On a more practical level, where would it sit? Possibly in a number of places – eg, major commercial and arbitration centres.

UNCITRAL could draft provisions relating to the establishment of the Court.

Functioning of CICA

CICA would be fundamental to the developing and upholding of international public policy, whilst, at the same time, providing a consistency of approach in the enforcement of awards.

It is essential that consistency, however desirable in itself, should nonetheless be underpinned by certain safeguards. The statute for CICA could include the bases on which public policy is to be applied.

It should be provided that CICA *must* take cognisance of concerns over such matters as corruption, illegality, immorality and unconscionable behaviour. (These may, of course, to a certain extent overlap). There should also be provisions covering the sources to which CICA must direct itself in order to ascertain not only the law, but to inform itself about international standards and norms. As noted above in this Chapter, the UN plays a vitally important role in shaping universal values. Reference could accordingly be made to UN Conventions and Declarations, as well as to the practices or declarations of other bodies concerned with international relations or trade, such as the OECD.

In the absence of any such provisions, the judges might simply adopt the narrow approach favoured by the United States.

To achieve balance, it should also be provided that the application of public policy can only derogate from the certainty created by the New York Convention to the extent necessary to protect the integrity of public institutions and to prevent parties from obtaining any benefit from immoral, illegal or unconscionable behaviour.

It would also fall to CICA to continue to mould public policy. Stone's reference to courts drawing on extra-legal sources was noted above. [46] Stone also notes that the empirical knowledge and values that courts draw on or refer to are contextual – those of a particular time and place. As times and places change, it must follow that community values and experience change as well. Consequently, CICA would need to remain alert to the evolution of international standards and norms, and fashion its outlook and responses accordingly.

Applicants must come to CICA acting in good faith

Whilst CICA itself would look for any possible conflict with public policy, applicants wishing to invoke its jurisdiction must act in good faith in doing so. This must apply to respondents, as well as applicants.

As good faith is an important component of contract law, it is appropriate that such a requirement be imposed. Commercial arbitration comes out of private bargains. A finding that a party was not acting in good faith could disqualify them from seeking enforcement.

In light of its so far limited application in the common law, not all parties may come under this obligation in their contracts, but, it is suggested, it is not unreasonable to expect everyone who approaches CICA to proceed in good faith. As was noted in Chapter IV, the Courts of New South Wales have held that a duty of good faith may be imposed by implication upon parties to a contract. In *Aiton v Transfield*, Einstein J of the Supreme Court of New South Wales suggested that, whilst definitions of good faith were often expressed in the negative (ie, the meaning of good faith is to be discerned by reference to examples of "bad faith" behaviour) there may nonetheless be "overarching 'core' principles of 'good faith'. [47] His Honour adopted a passage

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46 See Chapter IV.

47 op cit, at paragraph 132.

from Stapleton, [48] in which Stapleton suggests that good faith "restrains the deliberate pursuit of self-interest where this is judged unconscionable." This could include dishonesty, contradictory behaviour or exploiting a position of dominance. [49] This conceptual basis, it is suggested, could serve as a basis for the imposition of a duty to act in good faith.

CICA's place in the framework of international trade

Apart from constitutional and jurisdictional issues, there are practical questions of how CICA might function within the overall framework that sustains international trade - how it might function in the overall context of international trade and international economic relationships.

Abbott suggests that a model for "integrated governance" is evolving out of the relationship between the WTO and WIPO. [50] Each organisation is seen as being able to benefit from the ability to draw on each other's strengths and abilities, whilst, at the same time maintaining independence and objectivity about its own role. WIPO, for instance, is seen as being far more flexible and responsive to change than the WTO. The WTO can accordingly benefit by WIPO introducing changes to its approach to issues and procedures, changes which the WTO may not be able to effect within its own structure.

This model, the author suggests, could carry over to other circumstances. The WTO could, and should, develop more complementary relationships with institutions such as the United Nations Conference on Trade and Development, the World Health Organisation and the IMF.

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48 Stapleton, "Good Faith in Private Law", *Current Legal Problems*, [1999] Volume 52, at 1.
49 op cit, at 57.
50 Abbott, op cit, 63.

Abbott suggests that the formation of these informal relationships between the WTO and other institutions is essential, as the WTO:-

> " . . . is in a position to provide leadership in establishing a global economic system that provides reasonable measure of support to the countries which share least in the gains from trade and investment." [51]

Whether the provision of leadership does benefit the countries that "share the least" in the gains from trade is another matter. It has been suggested that whilst developing countries have received some benefits from liberalising trade, overall, their position was not greatly improved by the Uruguay Round. It was believed that the concessions (especially in the area of intellectual property) granted were not matched by commitments given by developed countries in relation to agriculture and textiles. [52]

The WTO might then be perceived as not providing appropriate leadership, at least as far as developing nations are concerned.

CICA would, therefore, need to carefully assess any "integrated" relationship with the WTO.

The WTO is certainly not the only organisation with which CICA could develop such relationships. UNCITRAL and UNCTAD are possible alternatives. The former has a legislative structure for commercial arbitration, and could benefit from CICA's perspective and experience in enforcing awards; the latter having responsibility for trade issues concerning developing nations, could provide CICA with the perspective from those countries.

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51 Abbott, op cit, 75.

52 Watal, "Developing Countries' Interests in a 'Development Round' " in Schott, op cit, at 71 and 72.

The key for CICA would be to maintain its objectivity and independence whilst drawing on these other organisations for knowledge and experience.

Conclusions

The processes of commercial arbitration are coming under pressure to become more "efficient", more global. This suits the economically powerful trading nations who are the ones to benefit most from the "uniform" approach.

The increasing privatisation of international dispute resolution must not be allowed to lead to the negation of the public interest. Public policy must continue to play a key role. It must be allowed to do so. Cases such as *Westacre* indicate that there are dangers in seeking to promote efficiency over principle and the public interest. Arbitrations such as *Sandline* demonstrate the possible dangers of ignoring international concerns.

The observation by Lew to the effect that arbitrators are the private guardians of international trade was noted in Chapter IV and above in this Chapter. It is worth considering a more expansive quote:-

> " . . . the obligations of arbitrators, accepted as private guardians of international commercial transactions and the developers of the *lex mercatoria*, [are] to uphold the fundamental and accepted standards of international trade and *not to fall into the role of enforcing international practices regardless of whether they concur with prevailing applicable law* and accepted international commercial standards. In this capacity, there is justification for the arbitrator to react to a manifest violation of international public policy, *even though the issue has not been raised by either party*." [53] (emphasis added).

This confirms the strict duty on arbitrators to apply public policy. That duty transcends the relationship between the arbitrator and the disputants. Private processes must not be utilised or manipulated to conceal questions of significant public concern.

Courts must also adhere to their duty - they must be vigilant to ensure the integrity of arbitration is maintained.

As Cardozo stated:-

> "Implicit in every decision where the question is, so to speak, at large, is a philosophy of the origin and aim of law. . . ". [54]

A vitally important factor in ensuring that prevailing values are reflected in both awards and judgments is the duty to apply public policy, free of any restrictions.

The challenge is to move away from the present approach of narrowing (or ignoring altogether) the operation of public policy. Unless this is done, the integrity of arbitration, together with that of institutions which are called upon to support arbitration, may be in doubt.

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53 Lew, *Contemporary Problems*, op cit, at 85.
54 Cardozo, *The Growth of the Law*, op cit, at 25, 26.

APPENDICES

APPENDIX "A"

Convention on the Recognition and Enforcement of Foreign Arbitral awards ("New York Convention")

Article 1

1. This Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought and arising out of differences between persons, whether physical or legal. It shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought.

2. The term "arbitral awards" shall include not only awards made by arbitrators appointed for each case but also those made by permanent arbitral bodies to which the parties have submitted.

3. When signing, ratifying or acceding to this Convention, or notifying extension under article X hereof, any State may on the basis of reciprocity declare that it will apply the Convention to the recognition and enforcement of awards made only in the territory of another Contracting State. It may also declare that it will apply the Convention only to differences arising out of legal relationships, whether contractual or not, which are considered as commercial under the national law of the State making such declaration.

Article II

1. Each Contracting State shall recognise an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may

arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.

2. The term "agreement in writing" shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.

3. The court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed.

Article III

Each Contracting State shall recognise arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, under the conditions laid down in the following articles. There shall not be imposed substantially more onerous conditions or higher fees or charges on the recognition or enforcement of arbitral awards to which this Convention applies than are imposed on the recognition or enforcement of domestic arbitral awards.

Article IV

1. To obtain the recognition and enforcement mentioned in the preceding article, the party applying for recognition and enforcement shall, at the time of the application, supply:

   (a) The duly authenticated original award or a duly certified copy thereof;

   (b) The original agreement referred to in article II or a duly certified copy thereof.

2. If the said award or agreement is not made in an official language of the country in which the award is relied upon, the party applying for recognition and enforcement of the award

shall produce a translation of these documents into such language. The transaction shall be certified by an official or sworn translator or by a diplomatic or consular agent.

Article V

1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:

(a) The parties to the agreement referred to in article II were, 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; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced; or

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(e) The award has not yet become binding, on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.

Article VI

If an application for the setting, aside or suspension of the award has been made to a competent authority referred to in article V (1) (e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award and may also, on the application of the party claiming enforcement of the award, order the other party to give suitable security.

Article VII

1. The provisions of the present Convention shall not affect the validity of multilateral or bilateral agreements concerning the recognition and enforcement of arbitral awards entered into by the Contracting States nor deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law or the treaties of the country where such award is sought to be relied upon.

2. The Geneva Protocol on Arbitration Clauses of 1923 and the Geneva Convention on the Execution of Foreign Arbitral Awards of 1927 shall cease to have effect between Contracting States on their becoming bound and to the extent that they become bound, by this Convention.

Article VIII

1. This Convention shall be open until 31 December 1958 for signature on behalf of any Member of the United Nations and also on behalf of any other State which is or hereafter becomes a member of any specialised agency of the United Nations, or which is or hereafter becomes a party to the Statute of the International Court of Justice, or any other State to which an invitation has been addressed by the General Assembly of the United Nations.

2. This Convention shall be ratified and the instrument of ratification shall be deposited with the Secretary-General of the United Nations.

Article IX

1. This Convention shall be open for accession to all States referred to in article VIII.

2. Accession shall be effected by the deposit of an instrument of accession with the Secretary-General of the United Nations.

Article X

1. Any State may, at the time of signature, ratification or accession, declare that this Convention shall extend to all or any of the territories for the international relations of which it is responsible. Such a declaration shall take effect when the Convention enters into force for the State concerned.

2. At any time thereafter any such extension shall be made by notification addressed to the Secretary-General of the United Nations and shall take effect as from the ninetieth day after the day of receipt by the Secretary-General of the United Nations of this notification, or as from the date of entry into force of the Convention for the State concerned, whichever is the later.

3. With respect to those territories to which this Convention is not extended at the time of signature, ratification or accession, each State concerned shall consider the possibility of taking the necessary steps in order to extend the application for this Convention to such territories, subject, where necessary for constitutional reasons, to the consent of the Governments of such territories.

Article XI

In the case of a federal or non-unitary State, the following provisions shall apply:

(a) With respect to those articles of this Convention that come within the legislative jurisdiction of the federal authority, the obligations of the federal Government shall to this extent be the same as those of Contracting States which are not federal States;

(b) With respect to those articles of this Convention that come within the legislative jurisdiction of constituent states or provinces which are not, under the constitutional system of the federation, bound to take legislative action, the federal Government shall bring such articles with a favourable recommendation to the notice of the appropriate authorities of constituent states or provinces at the earliest possible moment;

(c) A federal State Party to this Convention shall, at the request of any other Contracting State transmitted through the Secretary-General of the United Nations, supply a statement of the law and practice of the federation and its constituent units in regard to any particular provision of this Convention, showing the extent to which effect has been given to that provision by legislative or other action.

Article XII

1. This Convention shall come into force on the ninetieth day following the date of deposit of the third instrument of ratification or accession.

2. For each State ratifying or acceding to this Convention after the deposit of the third instrument of ratification or accession, this Convention shall enter into force on the ninetieth day after deposit by such State of its instrument of ratification or accession.

Article XIII

1. Any Contracting State may denounce this Convention by a written notification to the Secretary-General of the United Nations. Denunciation shall take effect one year after the date of receipt of the notification by the Secretary-General.

2. Any State which has made a declaration or notification under article X may, at any time thereafter, by notification to the Secretary-General of the United Nations, declare that this Convention shall cease to extend to the territory concerned one year after the date of the receipt of the notification by the Secretary-General.

3. This Convention shall continue to be applicable to arbitral awards in respect of which recognition or enforcement proceedings have been instituted before the denunciation takes effect.

Article XIV

A Contracting State shall not be entitled to avail itself of the present Convention against other Contracting States except to the extent that it is itself bound to apply the Convention.

Article XV

The Secretary-General of the United Nations shall notify the States contemplated in article VIII of the following:

(a) Signatures and ratifications in accordance with article VIII;

(b) Accessions in accordance with article IX;

(c) Declarations and notifications under articles I, X and XI;

(d) The date upon which this Convention enters into force in accordance with article XII;

(e) Denunciations and notifications in accordance with article XIII.

Article XVI

1. This Convention, of which the Chinese, English, French, Russian and Spanish texts shall be equally authentic, shall be deposited in the archives of the United Nations.

2. The Secretary-General of the United Nations shall transmit a certified copy of this Convention to the States contemplated in article VIII.

APPENDIX "B"

UNCITRAL Model Law on International Commercial Arbitration ("UNCITRAL Model Law")

CHAPTER 1 - GENERAL PROVISIONS

Article 1 - Scope of application

1. This Law applies to international commercial arbitration, subject to any agreement in force between this State and any other State or States.

2. The provisions of this Law, except articles 8, 9, 35 and 36, apply only if the place of arbitration is in the territory of this State.

3. An arbitration is international if:

   (a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or

   (b) one of the following places is situated outside the State in which the parties have their places of business:

      (i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;

      (ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected; or

(c) the parties have expressly agreed that the subject-matter of the arbitration agreement relates to more than one country.

4. For the purposes of paragraph (3) of this article:

(a) if a party has more than one place of business, the place of business is that which has the closest relationship to the arbitration agreement;

(b) if a party does not have a place of business, reference is to be made to his habitual residence.

5. This Law shall not affect any other law of this State by virtue of which certain disputes may not be submitted to arbitration or may be submitted to arbitration only according to provisions other than those of this Law.

Article 2 - Definitions and rules of interpretation

For the purposes of this Law:

(a) "arbitration" means any arbitration whether or not administered by a permanent arbitral institution;

(b) "arbitral tribunal" means a sole arbitrator or a panel of arbitrators;

(c) "court" means a body or organ of the judicial system of a State;

(d) where a provision of this Law, except article 28, leaves the parties free to determine a certain issue, such freedom includes the right of the parties to authorise a third party, including an institution, to make that determination;

(e) where a provision of this Law refers to the fact that the parties have agree or that they may agree or in any other way refers to an agreement of the parties; such agreement includes any arbitration rules referred to in that agreement;

(f) where a provision of this Law, other than in articles 25(a) and 32(2)(a), refers to a claim, it also applies to a counter-claim and where it refers to a defence, it also applies to a defence to such counter-claim.

Article 3 - Receipt of written communications

1. Unless otherwise agreed by the parties:

   (a) any written communication is deemed to have been received if it is delivered to the addressee personally or if it is delivered at his place of business, habitual residence or mailing address; if none of these can be found after making a reasonable inquiry, a written communication is deemed to have been received if it is sent to the address's last-known place of business, habitual residence or mailing address by registered letter or any other means which provides a record of the attempt to deliver it;

   (b) the communication is deemed to have been received on the day it is so delivered.

2. The provisions of this article do not apply to communications in court proceedings.

Article 4 - Waiver of right to object

A party who knows that any provision of this Law from which the parties may derogate or any requirement under the arbitration agreement has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance without undue delay or, if a time-limit is provided therefor, within such period of time, shall be deemed to have waived his right to object.

Article 5 - Extent of court intervention

In matters governed by this Law, no court shall intervene except where so provided in this Law.

Article 6 – Court or other authority for certain functions of arbitration assistance and supervision

The functions referred to in articles 11(3), 11(4), 13(3), 14, 16(3) and 34(2) shall be performed by [Each State enacting this model law specifies the court, courts or, where referred to therein, other authority competent to perform these function].

CHAPTER II – ARBITRATION AGREEMENT

Article 7 - Definition and form of arbitration agreement.

1. "Arbitration agreement" is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

2. The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement, or in an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by another. The reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause part of the contract.

Article 8 – Arbitration agreement and substantive claim before court

1. A court before which an auction is brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is real and void, inoperative or incapable of being performed.

2. Where an auction referred to in paragraph (1) of this article has been brought, arbitral proceedings may nevertheless be commenced or continued and an award may be made, while the issue is pending before the court.

Article 9 - Arbitration agreement and interim measures by court

It is not incompatible with any arbitration agreement for a party to request, before or during arbitral proceedings, from a court an interim measure of protection and for a court to grant such measure.

CHAPTER III - COMPOSITION OF ARBITRAL TRIBUNAL

Article 10 - Number of arbitrators

1. The parties are free to determine the number of arbitrators.

2. Failing such determination, the number of arbitrators shall be three.

Article II - Appointment of arbitrators

1. No person shall be precluded by reason of his nationality from acting as an arbitrator, unless otherwise agreed by the parties.

2. The parties are free to agree on a procedure of appointing the arbitrator or arbitrators, subject to the provisions of paragraphs (4) and (5) of this article.

3. Failing such agreement:

   (a) in an arbitration with three arbitrators, each party shall appoint one arbitrator and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the third arbitrator within thirty days of receipt of a request to do so from the other party, of if the two arbitrators fail to agree on the third arbitrator within thirty days of their appointment, the appointment shall be made, upon request of a party, by the court or other authority specified in article 6;

(b) in an arbitration with a sole arbitrator, if the parties are unable to agree on the arbitrator, he shall be appointed, upon request of a party, by the court or other authority specified in article 6.

4. Where, under an appointment procedure agreed upon by the parties:

(a) a party fails to act as required under such procedure, or

(b) the parties, or two arbitrators, are unable to reach an agreement expected of them under such procedure, or

(c) a third party, including an institution, fails to perform any function entrusted to it under such procedure,

(d) any party may request the court or other authority specified in article 6 to take the necessary measure, unless the agreement on the appointment procedure provides other means for securing the appointment.

5. A decision on a matter entrusted by paragraph (3) and (4) of this article to the court or other authority specified in article 6 shall be subject to no appeal. The court or other authority, in appointing an arbitrator, shall have due regard to any qualifications required of the arbitrator by the agreement of the parties and to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality other than those of the parties.

Article 12 – Grounds for challenge

1. When a person is approached in connection with his possible appointment as an arbitrator, he shall disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay disclose any such circumstances to the parties unless they have already been informed of them by him.

2. An arbitrator may be challenged only if circumstances exist that give rise to justifiable doubts as to his impartiality or independence, or if he does not possess qualifications agreed to by the parties. A party may challenge an arbitrator appointed by him, or in whose appointment he has participated, only for reasons of which he becomes aware after the appointment has been made.

Article 13 – Challenge procedure

1. The parties are free to agree on a procedure for challenging an arbitrator, subject to the provisions of paragraph (3) of this article.

2. Failing such agreement, as party which intends to challenge an arbitrator shall, within fifteen days after becoming aware of the constitution of the arbitral tribunal or after becoming aware of the constitution of the arbitral tribunal or after becoming aware of any circumstance referred to in article 12(2), send a written statement of the reasons for the challenge to the arbitral tribunal. Unless the challenged arbitrator withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.

3. If a challenge under any procedure agreed upon by the parties or under the procedure of paragraph (2) of this article is not successful, the challenging party may request, within thirty days after having received notice of the decision rejecting the challenge, the court or other authority specified in article 6 to decide on the challenge, which decision shall be subject to no appeal; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings and make an award.

Article 14 – Failure or impossibility to act

1. If an arbitrator becomes de jure or de facto unable to perform his functions or for other reasons fails to act without undue delay, his mandate terminates if he withdraws from his office or if the parties agree on the termination. Otherwise, if a controversy remains concerning any of these grounds, any party may request the court or other authority specified in article 6 to decide on the termination of the mandate, which decision shall be subject to no appeal.

2. If, under this article or article 13(2), an arbitrator withdraws from his office or a party agrees to the termination of the mandate of an arbitrator, this does not imply acceptance of the validity of any ground referred to in this article or article 12(2).

Article 15 – Appointment of substitute arbitrator

Where the mandate of an arbitrator terminates under article 13 or 14 or because of his withdrawal from office for any other reason or because of the revocation of his mandate by agreement of the parties or in any other case of termination of his mandate, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitrator being replaced.

CHAPTER IV – JURISDICTION OF ARBITRAL TRIBUNAL

Article 16 – Competence of arbitral tribunal to rule on its jurisdiction

1. The arbitral tribunal may rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement. For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail ipso jure the invalidity of the arbitration clause.

2. A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence. A party is not precluded from raising such a plea

by the fact that he has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings. The arbitral tribunal may, in either case, admit a later plea if it considers the delay justified.

3. The arbitral tribunal may rule on a plea referred to in paragraph (2) of this article either as a preliminary question or in an award on the merits. If the arbitral tribunal rules as a preliminary question that it has jurisdiction, any party may request, within thirty days after having received notice of that ruling, the court specified in article 6 to decide the matter, which decision shall be subject to no appeal; while such a request is pending, the arbitral tribunal may continue the arbitral proceedings and make an award.

Article 17 – Power of arbitral tribunal to order interim measures

Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order any party to take such interim measure of protection as the arbitral tribunal may consider necessary in respect of the subject matter of the dispute. The arbitral tribunal may require any party to provide appropriate security in connection with such measure.

CHAPTER V – CONDUCT OF ARBITRAL PROCEEDINGS

Article 18 – Equal treatment of parties

The parties shall be treated with equality and each party shall be given a full opportunity of presenting his case.

Article 19 – Determination of rules of procedure

1. Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

2. Failing such agreement, the arbitral tribunal may, subject to the provisions of this Law, conduct the arbitration in such manner as it considers appropriate. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality and weight of any evidence.

Article 20 – Place of arbitration

1. The parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal having regard to the circumstances of the case, including the convenience of the parties.

2. Notwithstanding the provisions of paragraph (1) of this article, the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property or documents.

Article 21 – Commencement of arbitral proceedings

Unless otherwise agreed by the parties, the arbitral proceedings in respect of a particular dispute commence on the date on which a request for that dispute to be referred to arbitration is received by the respondent.

Article 22 – Language

1. The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any hearing and any award, decision or other communication by the arbitral tribunal.

2. The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or languages agreed upon by the parties or determined by the arbitral tribunal.

Article 23 – Statements of claim and defence

1. Within the period of time agreed by the parties or determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought and the respondent shall state his defence in respect of these particulars, unless the parties have otherwise agreed as to the required elements of such statements.

2. Unless otherwise agreed by the parties, either party may amend or supplement his claim or defence during the course of the arbitral proceedings, unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it.

Article 24 – Hearings and written proceedings

1. Subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether to hold oral hearings for the presentation of evidence or for oral argument, or whether the proceedings shall be conducted on the basis of documents and other materials. However, unless the parties have agreed that no hearings shall be held, the arbitral tribunal shall hold such hearings at an appropriate stage of the proceedings, if so requested by a party.

2. The parties shall be given sufficient advance notice of any hearing and of any meeting of the arbitral tribunal for the purposes of inspection of goods, other property or documents.

3. All statements, documents or other information supplied to the arbitral tribunal by one party shall be communicated to the other party. Also any expert report or evidentiary document on which the arbitral tribunal may rely in making its decision shall be communicated to the parties.

Article 25 – Default of a party

Unless otherwise agreed by the parties if, without showing sufficient cause:

(a) the claimant fails to communicate his statement of claim in accordance with article 23(1), the arbitral tribunal shall terminate the proceedings;

(b) the respondent fails to communicate his statement of defence in accordance with article 23(1), the arbitral tribunal shall continue the proceedings without treating such failure in itself as an admission of the claimant's allegations;

(c) any party fails to appear at a hearing or to produce documentary evidence, the arbitral tribunal may continue the proceedings and make the award on the evidence before it.

Article 26 – Expert appointed by arbitral tribunal

1. Unless otherwise agreed by the parties, the arbitral tribunal:

   (a) may appoint one or more experts to report to it on specific issues to be determined by the arbitral tribunal;

   (b) may require a party to give the expert any relevant information or to produce, or to provide access to, any relevant documents, goods or other property for his inspection.

2. Unless otherwise agreed by the parties, if a party so requests or if the arbitral tribunal considers it necessary, the expert shall, after delivery of his written or oral report, participate in a hearing where the parties have the opportunity to put questions to him and to present expert witnesses in order to testify on the points at issue.

Article 27 – Court assistance in taking evidence

The arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking evidence. The court may execute the request within its competence and according to its rules on taking evidence.

CHAPTER VI - MAKING OF AWARD AND TERMINATION OF PROCEEDINGS

Article 28 - Rules applicable to substance of dispute

1. The arbitral tribunal shall decide the dispute in accordance with such rules of law as are chosen by the parties as applicable to the substance of the dispute. Any designation of the law or legal system of a given State shall be construed, unless otherwise expressed, as directly referring to the substantive law of that State and not to its conflict of laws rules.

2. Failing any designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rules which it consider applicable.

3. The arbitral tribunal shall decide ex aequo et bono or as amiable compositeur only if the parties have expressly authorised to do so.

4. In all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction.

Article 29 - Decision - making by panel of arbitrators

In arbitral proceedings with more than one arbitrator, any decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, questions of procedure may be decided by a presiding arbitrator, if so authorised by the parties or all members of the arbitral tribunal.

Article 30 - Settlement

1. If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral tribunal, record the settlement in the form of an arbitral award on agreed terms.

2. An award on agreed terms shall be made in accordance with the provisions of article 31 and shall state that it is an award. Such an award has the same status and effect as any other award on the merits of the case.

Article 31 - Form and contents of award

1. The award shall be made in writing and shall be signed by the arbitrator or arbitrators. In arbitrator proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall suffice, provided that the reason for any omitted signature is stated.

2. The award shall state the reasons upon which it is based, unless the parties have agreed that no reasons are to be given or the award is an award on agreed terms under article 30.

3. The award shall state its date and the place of arbitration as determined in accordance with article 20(1). The award shall be deemed to have been made at that place.

4. After the award is made, a copy signed by the arbitrators in accordance with paragraph (1) of this article shall be delivered to each party.

Article 32 - Termination of proceedings

1. The arbitral proceedings are terminated by the final award or by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

2. The arbitral tribunal shall issue an order for the termination of the arbitral proceedings when:

   (a) the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognises a legitimate interest on his part in obtaining a final settlement of the dispute;

   (b) the parties agree on the termination of the proceedings;

(c) the arbitral tribunal finds that the continuation of the proceedings has for any other reason become unnecessary or impossible.

3. The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34(4).

Article 33 – Correction of interpretation of award; additional award

1. Within thirty days of receipt of the award, unless another period of time has been agreed upon by the parties:

(a) a party, with notice to the other party, may request the arbitral tribunal to correct in the award any error in computation, any clerical or typographical errors or any errors of similar nature;

(b) if so agreed by the parties, a party, with notice to the other party, may request the arbitral tribunal to give an interpretation of a specific point or part of the award.

If the arbitral tribunal considers the request to be justified, it shall make the correction or give the interpretation within thirty days of receipt of the request. The interpretation shall form part of the award.

2. The arbitral tribunal may correct any error of the type referred to in paragraph (1)(a) of this article on its own initiative within thirty days of the day of the award.

3. Unless otherwise agreed by the parties, a party, with notice to the other party, may request, within thirty days of receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the award. If the arbitral tribunal considers the request to be justified, it shall make the additional award within sixty days.

4. The arbitral tribunal may extend, if necessary, the period of time within which it shall make a correction, interpretation or an additional award under paragraph (1) or (3) of this article.

5. The provisions of article 31 shall apply to a correction or interpretation of the award or to an additional award.

CHAPTER VII - RECOURSE AGAINST AWARD

Article 34 – Application for setting aside as exclusive recourse against arbitral award

1. Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

2. An arbitral award may be set aside by the court specified in article 6 only if:

   (a) the party making the application furnishes proof that:

      (i) a party to the arbitration agreement referred to in article 7 was 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 this State; or

      (ii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

      (iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or

      (iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Law from which the parties cannot

derogate, or, failing such agreement, was not in accordance with this Law; or

(b) the court finds that:

(i) the subject matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the award is in conflict with the public policy of this State.

3. An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received that award or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal.

4. The court, when asked to set aside an award, may, where appropriate and so requested by a party, suspend the setting aside proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the arbitral tribunal's opinion will eliminate the grounds for setting aside.

CHAPTER VIII – RECOGNITION AND ENFORCEMENT OF AWARDS

Article 35 – Recognition and enforcement

1. An arbitral award, irrespective of the country in which it was made, shall be recognised as binding and, upon application in writing to the competent court, shall be enforced subject to the provisions of this article and of article 36.

2. The party relying on an award or applying for its enforcement shall supply the duly authenticated original award or a duly certified copy thereof and the original arbitration agreement referred to in article 7 or a duly certified copy thereof. If the award or agreement is not made in an official language of this State, the party shall supply a duly certified translation thereof into such language.

Article 36 – Grounds for refusing recognition or enforcement

1. Recognition or enforcement of an arbitral award, irrespective of the country in which it was made, may be refused only:

(a) at the request of the party against whom it is invoked, if that party furnishes to the competent court where recognition or enforcement is sought proof that:

(i) a party to the arbitration agreement referred to in article 7 was 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; or

(ii) the party against whom the award is invoked was not given proper notice of the appointment of an arbitrator or of the arbitrator proceedings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced; or

(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(v) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or

(b) if the court finds that:

(i) the subject matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the recognition or enforcement of the award would be contrary to the public policy of this State.

2. If an application for setting aside or suspension of an award has been made to a court referred to in paragraph (1)(a)(v) of this article, the court where recognition or enforcement is sought may, if it considers it proper, adjourn its decision and may also, on the application of the party claiming recognition or enforcement of the award, order the other party to provide appropriate security.

APPENDIX "C"

Agreement for the Provision of Military Assistance
Dated this 31 Day of January 1997 [1]

BETWEEN
The independent State of Papua New Guinea

AND

Sandline International

THIS Agreement is made this day of January 1997 between the Independent State of Papua New Guinea (the State) of the one part and Sandline International (Sandline), whose UK representative office is 535 Kings Road, London SW10 OSZ, of the other part.

WHEREAS

Sandline is a company specialising in rendering military and security services of an operational, training and support nature, particularly in situations of internal conflict and only for and on behalf of recognised Governments, in accord with international doctrines and in conformance with the Geneva Convention.
The State, engulfed in a state of conflict with the illegal and unrecognised Bougainville Revolutionary Army (BRA), requires such external military expertise to support its Armed Forces in the protection of its Sovereign territory and regain control over important national assets, specifically the Panguna mine. In particular, Sandline is contracted to provide personnel and related services and equipment to:

- train the State's Special Forces Unit (SFU) in tactical skills specific to the objective;
- gather intelligence to support effective deployment and operations;

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1 Obtained from theage.com.au 7 March 2000. Minor spelling errors have been corrected.

- conduct offensive operations in Bougainville in conjunction with PNG defence forces to render the BRA military ineffective and repossess the Panguna mine; and
- provide follow-up operational support, to be further specified and agreed between the parties and is subject to separate service provision levels and fee negotiations.

IT IS THEREFORE AGREED AS FOLLOWS:

The State hereby agrees to contract and utilise and employ the services of Sandline to provide all required and necessary services as are more particularly described hereafter.

Duration and Continuation

The duration of this contract shall be effective from the date of receipt of the initial payment, as defined in paragraph 5.2 below, for a maximum initial period of three calendar months (the initial contract period) or achievement of the primary objective, being the rendering of the BRA militarily ineffective, whichever is the earlier. The State shall have the option of renewing this agreement either in part or in whole for further periods as may be required.
Notice of renewal, termination or proposed variation of this agreement is to be served on Sandline in writing by the State at least 45 days before the expiry of the current period. Non-communication by the State shall be regarded by Sandline as automatic renewal of the relevant parts of this agreement for a further three months period on the same terms and this precedent shall continue to apply thereafter.

Service Provision

Sandline shall provide the following manpower, equipment and services:

(a) A 16 man Command, Admin and Training Team (CATT), to deploy in PNG and establish home bases at Jackson Airport and the Jungle Training Centre at Wewak within one week of commencement of this agreement, which is deemed to be the date on which the initial payment relating thereto in accordance with paragraph 5.2 below is deposited free and clear in Sandline's nominated bank account. The role of the CATT is to (i) establish links with PNG defence forces, (ii) develop the requisite logistics and communications infrastructure, (iii) secure and prepare facilities for the arrival of the contracted equipment, including air assets, (iv) initiate intelligence gathering operations and (v) commence SFU training.

(b) Further Special Forces personnel which will deploy to PNG within 10 days of the arrival of the CATT, together with helicopter and fixed wing aircrew and engineers, intelligence and equipment operatives, mission operators, ground tech and medical support personnel. This force will absorb the CATT as part of its number, therefore bringing the total Strike Force headcount to 70. This Strike Force shall be responsible for achieving the primary objective as specified in paragraph 1.1 of this agreement and the full complement will remain in country for the initial contract period as defined in the said paragraph.

Note: at no time will Sandline personnel enter the sovereign territory of another nation nor will they breach the laws and rules of engagement relating to armed conflict. Once the operation has been successfully concluded, Sandline personnel will be available to assist with the ongoing training, skills enhancement and equipping of the PNG defence forces.

(c) Weapons, ammunition and equipment, including helicopters and aircraft (serviceable for up to 50 hours flying time per machine per month) and electronic warfare equipment and communications systems, all as specified or equivalent to the items listed in Schedule 1. Upon termination of a contractual relationship between the State and Sandline and once all payments have been received and Sandline has withdrawn from theatre any remaining stock of equipment shall be handed over and become the property of the State. Selected Sandline personnel will remain in country to maintain and supplement such equipment subject to a separate agreement relating thereto.

Note: delivery into theatre of the contracted equipment shall be via air into Jackson Airport or such other facility as may considered appropriate. The equipment will be delivered in full working order in accordance with manufacturers' specifications. After its delivery, any equipment lost, damaged or destroyed during Sandline's deployment shall be immediately shall be immediately replaced at the cost of the State.

(d) Personal kit, including US pattern jungle fatigues, boots and webbing, for Sandline personnel.

(e) All international Transport arrangements for the shipment in/out of equipment and deployment in country of Sandline personnel but not for the movement of such equipment and personnel within the country if this needs to be achieved by way of commercial service providers.

(f) The provision of medical personnel to treat any Sandline casualties and their evacuation if necessary.

(g) A Project Co-ordinator who, together with the Strike Force Commander and his Senior Intelligence Officer, shall maintain liaison with and provide strategic and operational briefings and advice to the Prime Minister, Defence Minister, NEC, NSC, the commander of the PNG defence forces and his delegated officers as may from time-to-time be required or requested.

Sandline shall ensure the enrolment of all personnel involved in this contract as Special Constables and that they carry appropriate ID cards in order to legally undertake their assigned roles.

Responsibilities of Sandline

Sandline will train the SFU in tactical skills specific to the objective, such as live fire contact, ambush techniques and raiding drills, gather intelligence to support effective deployment and, plan, direct, participate in and conduct such ground, air and sea operations which are required to achieve the primary objective.

Both parties hereto recognise and agree that the force capability to respond to all emergency and hostile situations will be constrained by the manpower and equipment level provided within the terms of this agreement. The achievement of the primary objective cannot be deemed to be a performance measure for the sake of this agreement if it can be demonstrated that for valid reasons it cannot be achieved within the given timescale and with the level of contracted resources provided.

Sandline shall supply all the personnel and maintain all services and equipment as specified in paragraph 2.1 above to the appropriate standards of proficiency and operational levels as is generally expected from a high calibre, professional armed force.

Sandline shall further provide a project co-ordinator to act as the liaison officer between the company's management and the nominated representatives of the State. This individual will convene and attend regular meetings at such venues as he may be so directed.

Sandline shall be responsible for any expense resulting from the loss or injury of any of its personnel for the duration of the agreement unless same is caused by the negligence of the State,

its personnel or agents in which case all such costs will be fairly claimed against the State by Sandline and promptly paid for the benefit of the persons involved.

Sandline will ensure that the contents of this agreement shall remain strictly confidential and will not be disclosed to any third party. Sandline will not acknowledge the existence of his contract prior to the State issuing notifications in accordance with paragraph 4.11 below and will not take credit for any successful action unless this is mutually agreed by the parties. Furthermore, Sandline and its personnel are well versed in the requirement to maintain absolute secrecy with regard to all aspects of its activities in order to guard against compromising operations and will apply the necessary safeguards.

Responsibilities of the State

Immediately on signing this agreement the State automatically grants to Sandline and its personnel all approvals, permissions, authorisations, licences and permits to carry arms, conduct its operations and meet its contractual obligations without hindrance, including issuing instructions to PNG defence forces personnel to co-operate fully with Sandline commanders and their nominated representatives. All officers and personnel of Sandline assigned to this contract shall be enrolled as Special Constables, but hold military ranks commensurate with those they hold within the Sandline command structure and shall be entitled to given orders to junior ranks as may be necessary for the execution of their duties and responsibilities.

The State will ensure that full co-operation is provided from within its organisation and that of the PNG defence forces. The Commanders of the PNG defence forces and Sandline shall form a joint liaison and planning team for the duration of this agreement. The operational deployment of Sandline personnel and equipment is to be jointly determined by the Commander, PNG defence forces and Sandline's commander, taking account of their assessment of the risk and value thereof.

The State recognises that Sandline's commanders will have such powers as are required to efficiently and effectively undertake their given roles, including but not limited to the powers to engage and fight hostile forces, repel attacks therefrom, arrest any persons suspected of undertaking or conspiring to undertake a harmful act, secure Sovereign assets and territory, defend the general population from any threat and proactively protect their own and State Forces from any form of aggression or threat. The State agrees to indemnify Sandline for the legitimate

actions of the company's and its associates' personnel as specified herein and to assume any claims brought against the company arising out of this agreement.

The State shall pay or shall cause to be paid the fees and expenses relating to this agreement as set out in paragraph 5.1 below. Such fees and expenses to be paid as further specified in paragraph 5.2, without deduction of any taxes, charges or fees and eligible to be freely exported from PNG. All payments to be made in US Dollars.

The State shall cause all importation of equipment and the provision of services to be free to Sandline (and any of its sister or associated companies as notified to the authorities) of any local, regional or national taxes, withholding taxes, duties, fees, surcharges, storage charges and clearance expenses howsoever levied and shall allow such equipment to be processed through Customs without delay. Further, all Sandline personnel will be furnished with the necessary multiple entry visas without passport stamps and authorisation to enter and leave the country free from hindrance at any time and shall be exempt from tax of any form on their remuneration from Sandline.

The State will promptly supply at no cost to Sandline and its sister and associated companies all End User Certificates and related documentation to facilitate the legitimate procurement and export of the specified equipment from countries or origin.

The State will provide suitable accommodation for al Sandline personnel together with all related amenities, support staff to undertake roles such as messengers and household duties, secure hangerage and storage facilities for equipment, qualified tradesmen and workmen to clear and prepare operating sites, all aviation and ground equipment fuel and lubricant needs, such vehicles and personnel carriers as reasonably specified for the field and for staff use, foodstuffs and combat rations, fresh drinking water and sanitary and other relevant services and ancillary equipment as Sandline may specify from time to time to undertake its activities without hindrance.

If any service, resource or equipment to be supplied by the State in accordance with paragraph 4.7 above is not forthcoming then Sandline will have the right to submit an additional invoice for the procurement and supply thereof and may curtail or reduce operations affected by its non-availability until payment has been made and the said equipment is in position.

The State agrees and undertakes that, during the period of this agreement and for a period of 12 months following the date of its expiration, it will not directly or indirectly offer employment to or employ any of the personnel provided hereunder or otherwise in the employ of Sandline and its associates. Any such employment will be constructed as a continuation of the contract for the employees concerned and Sandline shall be entitled to be paid accordingly on a pro-rata basis.

The State and the PNG defence forces will ensure that information relating to planned operations, deployments and associated activities is restricted to only those personnel who have an essential need to be briefed in. Appropriate steps will be taken to prevent press reporting, both nationally and internationally, or any form of security breach or passage of information which may potentially threaten operational effectiveness and/or risk the lives of the persons involved. Sandline's commanders have the right to curtail any or all planned operations which they determine are compromised as a result of failure in security.

If deemed necessary due to external interest, the State shall be responsible for notifying and updating the International Community, including the United Nations and representatives of other Governments, at the appropriate time of the nature of this contract and the underlying intent to protect and keep safe from harm Papua New Guinea's Sovereign territory, its population, mineral assets and investing community. The content and timing of all such formal communications will be discussed and agreed with Sandline before release.

Fees and Payments

Sandline's inclusive fee for the provision of the personnel and services as specified in paragraph 2.1 above and also in Schedule 1 attached for the initial contract period is USD36,000,000 (thirty six million US Dollars).

Payment terms are as follows. All payments to be by way of cash funds, either in the form of electronic bank transfers or certified banker's cheques.

On contract signing 50 per cent of the overall fee, totalling USD18,000,000 is immediately due and is deemed the "initial payment".

Within 30 days of deploying the CATT, the balance of USD18,000,000.

This contract is deemed to be enacted once the initial payment is received in full with value into such bank account as Sandline may nominate therefor. Payments are recognised as being received when they are credited as cleared funds in our account and payment receipt relies on this definition.

All fees for services rendered shall be paid in advance of the period to which they relate. Sandline reserves the right to withdraw from theatre in the event of non-payment of fees for any renewal to the original contract period.

The financial impact of variations, additions or charges to the personnel provision and equipment supply specified herein will be agreed between the parties and any incremental payment will be made to Sandline before such change is deemed to take effect. There is no facility for rebate or refund in the event of a required reduction or early termination of service delivery within a given contract period.

Applicable Law

In the event of any dispute or difference arising out of or in relation to this agreement the parties shall in the first instance make an effort to resolve it amicably, taking account of the sensitive nature of this arrangement.

The aggrieved party shall notify the other by sending a notice of dispute in writing and, where amicable settlement is not possible within 30 days thereafter, refer the matter to arbitration in conformity with the UNCITRAL rules applying thereto.

This agreement shall be construed and governed in accordance with the Laws of England and the language of communication between the parties shall be English.

Amendments and Supplements

This agreement may only be altered, modified or amended by the parties hereto provided that such alteration, modification or amendment is in writing and signed by both parties.
Schedule 1 ("Oyster" Costings) forms part of this agreement.

IN WITNESS WHEREOF the parties hereto have set their hands on the day and year first written above.

For the Independent State of Papua New Guinea:

Name: C.S (indecipherable)

Witness: (indecipherable)

Name: Vele Iamo

Occupation: A/Deputy Secretary

For Sandline International:

Name: Tim Spicer OBE.

Witness: (indecipherable)

Name: J.N. Van Den Bergh

Occupation: Consultant

In the matter of an International Arbitration Under the UNCITRAL Rules Between Sandline International Inc and the Independent State of Papua New Guinea [2]

(Interim award)

The Rt Hon Sir Edward Somers, The Rt Hon Sir Michael Kerr and The Hon Sir Daryl Dawson.

1. *Background*

The Panguna Copper Mine is situated on the island of Bougainville, which is part of the Independent State of Papua New Guinea (PNG). When it was operating, the mine employed some 4,000 people and provided 17% of the revenue of PNG. Late in 1988, a dispute arose between the Government of PNG and Bougainville landowners whose land had been resumed for the development of the mine. The dispute escalated in the following year when the landowners blew up power pylons, cutting off power to the mine and forcing it to shut down. A revolutionary movement subsequently grew out of the conflict, which was no longer confined to landowners, seeking the independence of Bougainville from PNG or, possibly, the union of Bougainville with the Solomon Islands. An armed struggle took place between the PNG Defence Force and a local force which had emerged and became known as the Bougainville Revolutionary Army (BRA). A number of persons, including civilians, were killed. The PNG Defence Force was unable to recover possession of the mine and the Government was forced to examine the military options for the resolution of the Bougainville problem. The PNG Defence Force lacked the necessary equipment, in particular, helicopter gunships, helicopter troop carriers and modern electronic warfare equipment. Consequently, the PNG Government looked for assistance outside PNG.

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2 International Law Reports, Volume 117, Cambridge University Press, 2000, at 552.

2. *The 1997 Agreement*

2.1 Negotiations took place between representatives of PNG and Sandline International Inc. (Sandline), a company incorporated in the Commonwealth of the Bahamas and carrying on business in the United Kingdom, which led to the conclusion of an Agreement dated 31 January 1997 between PNG and Sandline (hereinafter referred to as "the Agreement"). The nature of those negotiations is not material for present purposes, for it is not disputed that the Agreement was signed by Mr Haiveta, the Deputy Prime Minister of PNG, on behalf of PNG, with the knowledge and approval of the Prime Minister and the Minister for Defence and pursuant to a resolution of the National Executive Council of PNG which "approved the use of PNG Special Forces Unit with Sandline International on operations in Bougainville" and "approved US $36m. to engage Sandline International for the operations with the initial 50% [to] be paid and the remainder to be settled once operations commence". Approval was given in identical terms by the PNG National Security Council.

2.2 Sandline was described in the Agreement as:

> "a company specialising in rendering military and security services of an operational, training and support nature, particularly in situations of internal conflict and only for and on behalf of recognised Governments, in accord with international doctrines and in conformance with the Geneva Convention."

The Agreement recited that PNG was engulfed in a state of conflict with the BRA and required military assistance. It further recited that Sandline was contracted to provide personnel and related services and equipment to:

"- train the State's Special Forces Unit in tactical skills specific to the objective:

- gather intelligence to support effective deployment and operations;
- conduct offensive operations in Bougainville in conjunction with PNG defence forces to render the BRA military ineffective and repossess the Panguna mine; and

- provide follow-up operational support, to be further specified and agreed upon between the parties and is subject to separate service provision levels and fee negotiations."

For its part, PNG was to ensure full co-operation from within its organisation and that of the PNG defence forces.

2.3 Sandline's inclusive fee for the provision of personnel, equipment and services under the Agreement was specified as US$ 36 million. US $18 million was immediately due on the signing of the Agreement and was deemed "the initial payment". The balance of US $18 million was payable within 30 days of the deployment by Sandline of a sixteen man Command, Administration and Training Team in PNG. The initial payment of US $18 million was paid by PNG. Notwithstanding that the required Command, Administration and Training Team was deployed in the first week of the contract and that certain equipment was duly delivered, the balance of US $18 million was not, and has not been, paid.

2.4 It is only necessary to add that the Agreement provided that:

"6.1 In the event of any dispute or difference arising out of or in relation to this agreement the parties shall in the first instance make an effort to resolve it amicably, taking account of the sensitive nature of this arrangement.

6.2 The aggrieved party shall notify the other by sending a notice of dispute in writing and, where amicable settlement is not possible within 30 days thereafter, refer the matter to arbitration in conformity with the UNCITRAL rules applying thereto.

6.3 This agreement shall be construed and governed in accordance with the Laws of England and the language of communication between the parties shall be English."

2.5 The parties do not contest the Tribunal's jurisdiction under this clause to determine the dispute that has arisen between them. A proposed amendment to PNG's pleadings

challenging the validity of the clause and the Tribunal's jurisdiction was withdrawn at the first hearing.

3. *The Breakdown of the Agreement*

3.1 Until the evening of 16 March 1997, the parties were engaged in the performance of the Agreement in an apparently co-operative manner. On that evening, there was an insurrection or mutiny by members of the PNG Defence Force in Port Moresby, led by the Commander of the Force, General Singirok. The uprising was named "Operation Rausim Kwik". Sandline personnel were placed under arrest. The military forces involved were joined the next day by civilians and there were outbreaks of rioting and looting and something in the nature of a siege of the Parliament building. On 21 March 1997 Sandline personnel were, with one exception, flown out of PNG, the remaining member being allowed to leave shortly thereafter.

3.2 The Prime Minister of PNG "suspended" the Agreement and announced a judicial inquiry to establish the facts concerning the origins of the Agreement. A Commission of Inquiry reported on about 29 May 1997 without questioning Sandline's effective engagement under the Agreement. But on 3 June PNG alleged that the Agreement had been frustrated on the ground that its performance had become impossible.

4. *The Arbitration*

4.1 Pursuant to the arbitration clause in the agreement, Sandline claimed from PNG payment of the sum of US $18 million, being the second payment referred to in the Agreement. Sandline also claimed a further sum then standing at US $ 1.4 million on account of storage charges for the equipment delivered to locations in PNG and other equipment which was held up or diverted due to the suspension of the Agreement. PNG responded by claiming that the performance of the contract had become impossible and that, in the events that had happened, the contract had been frustrated, and counterclaimed for the return of the US $18 million paid by it on the signing of the Agreement pursuant to the English Law Reform (Frustrated Contracts) Act 1943 and denied any liability for the alleged storage charges. Both parties also claimed interest and costs.

4.2 On the pleadings as they originally stood, the principal issue was whether, as contended by PNG, the Agreement had been frustrated.

4.3 The arbitrators appointed by the parties were The Right Honourable Sir Michael Kerr and The Honourable Sir Daryl Dawson. They in turn and in accordance with Article 10(3)(a) of the UNCITRAL Model Law and Article 7 of the UNCITRAL Arbitration Rules, appointed The Right Honourable Sir Edward Somers to act as presiding arbitrator.

4.4 Sandline were represented throughout by Mr R Slowe and Ms T Blackwood of S.J. Berwin & Co. and by Mr Daniel Serota QC and Mr K. Nasir of counsel, and at the second hearing also by Professor Sir Elihu Lauterpacht QC and Mr I Griffin QC. PNG were originally represented by its Attorney-General, Mr S.R. Gabi and subsequently by his successor Mr M.M. Gene. Its counsel were originally Mr N.M. Cooke QC and Mr M.M. Varitimos and subsequently Mr R.V. Gyles QC and Mr D. Hammerschlag instructed by Holding Redlich. At the first hearing PNG's leading counsel was Mr Bathhurst QC and Mr D. Bennett QC at the second hearing.

4.5 The Tribunal directed a hearing at Cairns, a venue agreed by the parties and accepted as being the seat of the arbitration. The Tribunal also directed that such hearing be limited to the issue of liability so as to avoid lengthy and complicated arguments and the taking of accounts which, if the plea of frustration were to fail, would be a costly waste of time. The hearing was set down for 8 June 1998 and the following 13 working days.

4.6 Pursuant to Article 41 of the UNCITRAL Rules both parties made various payments into a bank account established in London for the purposes of the arbitration for the payment of the Tribunal's fees and expenses, and various payments were made therefrom to the Tribunal from time to time.

5. *The Proceedings*

5.1 The parties exchanged voluminous pleadings and written submissions together with the authorities relied on, as well as lengthy correspondence on procedural issues on which the Tribunal had to give rulings.

5.2 On 21 May 1998 PNG indicated its intention to apply to amend its Statement of Defence to plead that under the laws of PNG the contract was unlawful and that those who purported to enter into it on behalf of PNG lacked the capacity to do so. The Tribunal heard the application at the beginning of the hearing in Cairns on 8 June 1998 and, for the reasons then given, allowed the amendment. It directed that the costs of and occasioned by the amendment be borne by PNG. By way of security for these costs, PNG was directed to lodge 40,000 pounds sterling in the names of both parties in a bank in Australia. That direction was duly complied with.

5.3 The hearing upon the issues raised by the new pleading was deferred to enable Sandline to formulate its defence upon those issues. On 9 June PNG then opened its case upon the issue of frustration. This was followed by Sandline's submissions in response, whereupon PNG abandoned its defence of frustration.

5.4 On 10 June there was a hearing for directions for the future course of the arbitration. The hearing of the new issues of illegality and lack of capacity was adjourned to a date to be fixed. Subsequently, the Tribunal directed that hearing to commence in London on 6 July 1998. During the exchange of new pleadings, PNG abandoned its claim for the return of the sum of US $18 million already paid as an issue in the arbitration.

5.5 Daily transcripts were taken throughout the 3 days of the hearing in Cairns.

6. *The New Issues*

6.1 The new case for PNG, as set out in its Amended Defence, was that the agreement with Sandline was null and void, being at all times illegal and unlawful both in its formation and performance. The illegality alleged was that the agreement and its performance were in contravention of s.200 of the PNG Constitution, were in contravention of s.51 of the PNG Criminal Code and that performance of the agreement would entail contravention of s.7 of the PNG Firearms Act. It was further alleged by PNG that the Deputy Prime Minister who executed the agreement on behalf of PNG had no lawful authority to do so because of s.47 of the PNG Public Finances (Management) Act. Further, it was alleged that the agreement was beyond the power of PNG because of ss.11 and 47 of the PNG Constitution. In addition, PNG claimed that the agreement was void and unenforceable

because it was against the public policy of PNG and England and because it constituted an impermissible fetter upon various powers.

6.2 Sandline's reply was twofold. First, it said that upon the true construction of s.200 of Constitution, neither the agreement nor its intended performance was contrary to its provisions nor the provisions of any of the other statutes relied upon by PNG. Alternatively, Sandline said that English law, by which the contract was governed, included international law and that under such law, PNG could not, in the events which happened, rely upon s.200 of the Constitution or any of the other provisions upon which it sought to rely.

7. *The Further Proceedings*

The parties exchanged further lengthy pleadings and written submissions with further authorities directed to the new issues. The hearing of the new issues took place in London on 6, 7 and 8 July 1998. Daily transcripts were again taken. In addition to arguing the new issues, the parties made submissions and reached certain agreements about the form and contents of the Tribunal's Award to which further reference is made in paragraph 13 below.

8. *The First Issue*

8.1 Of the provisions relied upon by PNG, it placed most reliance upon s.200 of the Constitution. It provides as follows:

> "200. Raising unauthorized forces.
>
> (1) It is strictly forbidden to establish, equip, train or take part in military or paramilitary training, except such as is provided for by this Constitution, or to plan, prepare for or assist in the raising or training of such a force or in such training.
>
> (2) Subsection (1) does not prevent –

(a) the establishment of a reserve, auxiliary or special force (by whatever name known) as part of the Defence Force; or

(b) the establishment of civilian components of the Defence Force, or the establishment or recognition of non-combatant units or organizations within, attached to or associated with the Defence Force, in accordance with an Act of Parliament.

(3) An Act of Parliament may provide that Subsection (1) does not apply to the armed forces of any other country specified in or under the Act, or to the civilian components of, or to the non-combatant units or organizations whether attached to or associated with such forces."

8.2 The proper construction of s.200 of the PNG Constitution and its application in the circumstances of this case were the subject of argument before the Tribunal. However, the Tribunal is of the view that it is neither necessary nor desirable to express any final opinion upon the scope of the section, it being possible to reach a conclusion for the purposes of this Interim Award by assuming, without deciding, the illegality or unlawfulness under the section for which PNG contends. The scope and intent of s.200 is better left to the courts of PNG where knowledge and understanding of the local conditions give them a better and more accurate assessment of its effect. The same considerations apply to the other statutory provisions upon which PNG relied.

9. *English Law*

9.1 Under cl. 6.3 of the agreement between Sandline and PNG, which is set out above, the agreement is to be construed and governed in accordance with English law. PNG submits that English law will not lend its aid to the enforcement of a contract that is illegal in the place of performance if that place is a friendly country and the courts of that country would not enforce the contract. In that respect, it relies upon the cases of *Ralli Bros.* v. *Compania Naviera Y Azner* [1920] 2 KB 287; *Vita Food Products Inc.* v. *Unus Shipping Company Ltd (in liquidation)* [1939] AC 277 at 291; *Lemenda Trading Co. Ltd* v. *African Middle East Petroleum Co. Ltd* [1988] QB 448 at 459; *Regazzoni* v. *K. C. Sethia (1944) Ltd* [1958] AC 301[3] and *Foster* v. *Driscoll & Ors* [1929] 1 KB 470.[4]

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3 24 *ILR* 15.

9.2 The proposition upon which PNG relies clearly applies where the contract in question is between private parties. In such cases the principle is based upon public policy which is based in turn upon the comity of nations (see *Regazzioni* v. *K C Sethia (1944) Ltd* at 231). But where a contract is concluded by a state, one enters the realm of public international law and public policy wears a different aspect. For it is part of the public policy of England that its courts should give effect to clearly established rules of international law. See *Oppenheimer* v. *Cattermole* [1976 A.C. 249[5] at 278; *Trendtex Trading Company* v. *Central Bank of Nigeria* [1977] Q.B. 529[6] at 544; *Maclaine Watson & Co* v. *Department of Trade and Industry* [1988] 3 All E R 257[7] at 301,324. The principle is expressed in Oppenheim's *International Law* (9th ed), Vol 1, pp 55-56 as follows:

> "As regards the United Kingdom all such rules of customary international law as are universally recognised or have at any rate received the assent of this country are *per se* part of the law of the land. ...The application of international law as part of the law of the land means that, subject to the overriding effect of statute law, rights and duties flowing from rules of customary international law will be recognised and given effect by English Courts without the need for any specific act adopting those rules into English law."

The reference to statute law in this passage is, of course, a reference to English statute law and in the present case does not, contrary to a submission made by PNG, embrace the statute law of PNG.

10. *International Law*

10.1 The rules of international law in this case are clearly established and their application causes no difficulty. PNG submits that they have no application because the agreement between it and Sandline, a private party, does not attract international law. However, it is incontrovertible that PNG is an independent State and purported to contract in that

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4 4 *Ann Dig* 19.

5 72 *ILR* 446.

6 64 *ILR* 111 at 122.

capacity. An agreement between a private party and a State is an international, not a domestic, contract. This Tribunal is an international, not a domestic, arbitral tribunal and is bound to apply the rules of international law. Those rules are not excluded from, but form part of, English law, which is the law chosen by the parties to govern their contract. PNG cited no authority to support its submission and there is ample authority to the contrary. See, e.g., *George W. Hopkins (USA)* v. *United Mexican States*[8] (Day 1, p.56); *Setenave* v. *Settebello* (Day 1, p. 60); *LETCO* v. *Liberia*[9] (Day 1, p.70); *SPP* v. *Egypt*[10] (Day 1, p. 70); *Societé Ouest Africaine des Bétons Industriels (SOABI)* v. *State of Senegal* [1988] 2 ICSID Reports 190; *USA (on behalf of P. W. Shufeldt)* v *Guatemala* [1930] II RIAA 1079[11]; *In the Matter of Revere Copper and Brass Inc. and Overseas Private Investment Corporation* (1978) 56 *ILR* 258; *AMOCO International Finance Corporation* v. *Iran* (1987) 15 Iran-US CTR 189;[12] *Fromatome* v. *Atomic Energy Commission of Iran* (1983) VIII Yearbook of Commercial Arbitration 94; *Phillips Petroleum Company Iran* v *Iran* (1989) 21 IRAN-US CTR 79. The submission by PNG must be rejected.

10.2 In international law, in relation to contracts to which a State is a party and which are to be performed within the territory of that State, the principle and the authorities referred to in paragraph 9.1 above have no application or must at any rate give way to a fundamental qualification. This is that a State cannot rely upon its own internal laws as the basis for a plea that a contract concluded by it is illegal. It is a clearly established principle of international law that acts of a State will be regarded as such even if they are *ultra vires* or unlawful under the internal law of the State. Of course, a State is a juristic person and can only act through its institutions, officials or employees (commonly referred to in international law as organs). But their acts or omissions when they purport to act in their capacity as organs of the State are regarded internationally as those of the State even though they contravene the internal law of the State. See Oppenheim, *op. cit.*, pp. 84, 540. The Report of the International Law Commission to the United Nations (1975) vol. 2, *Yearbook of the International Law Commission*, p. 61 expressed the principle as follows:

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7 80 *ILR* 47.

8 3 *Ann Dig* 229.

9 89 *ILR* 313.

10 106 *ILR* 501.

11 5 *Ann Dig* 179.

12 83 *ILR* 500.

> "The characterization of certain conduct of organs as acts of the State for the purpose of determining its international responsibility is completely independent of the characterization of the same conduct as acts of the State liable to incur administrative responsibility under internal law."

In *Southern Pacific Properties (Middle East) Ltd* v. *Arab Republic of Egypt* 3 ICSID Reports 102,[13] the respondent submitted that it was not liable for certain acts of Egyptian officials which it said were legally non-existent or absolutely null and void according to Egyptian law. The Tribunal said at para. 85 of its award:

> "The principle of international law which the Tribunal is bound to apply is that which establishes the international responsibility of the State when unauthorized or *ultra vires* acts of officials have been performed by State agents under cover of their official character. If such unauthorized or *ultra vires* acts could not be ascribed to the State, all State responsibility would be rendered illusory. For this reason, ...the practice of states has conclusively established the international responsibility for unlawful acts of state organs, even if accomplished outside the limits of their competence and contrary to domestic law. (Sorensen (ed.), *Manual of Public International Law*, New York, 1968, at p.548)."

It is unnecessary to cite further authority for the principle, but other examples of its application are to be found in the cases referred to in paragraph 10.1 above.

10.3 The rules of international law referred to above are, of themselves, sufficient to dispose of the defence of illegality or unlawfulness raised by PNG. But there is the added rule that a party may not deny the validity of a contract entered into on its behalf by another if, by its conduct, it later consents to the contract. It is known as the doctrine of preclusion and, whether based upon the concepts of acquiescence, estoppel or waiver, is well established in international law. In the end the doctrine finds its justification in considerations of good faith and conscience which underlie the basic principle of international law, *pacta*

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[13] 106 *ILR* 501.

sunt servanda. See *R. N. Pomeroy* v. *Iran* (1983) 2 IRAN-US CTR 372 at 380; *The Shufeldt Claim* (1930) II RIAA 1079[14] at 1904; *Amoco International Finance Corporation* v. *Iran* (1987) 15 IRAN-US CTR 189[15] at 280-1; *Phillips Company Iran* v. *Iran* (1989) 21 IRAN-US CTR. 79 at 154-5. An apposite example is the *Shufeldt Claim*. In that case, the claimant entered into a contract with the Government of Guatemala for a chicle concession, the validity of which the government denied on the ground that it lacked the necessary approval of the legislature. The Tribunal said at p.1094:

> "In view of my finding that the contract was laid before the Legislature and approved by them, it is not necessary for me to deal with the second point raised by the United States case, viz., that the Guatemala Government having recognized the validity of the contract for six years and received all the benefits to which they were entitled under the contract and allowed Shufeldt to go on spending money on the concession, is precluded from denying its validity, even if the approval of the legislature had not been given to it.
>
> I may however state on this point that in all the circumstances I have related and the whole case submitted to me, I have no doubt that this contention of the United States is sound and in keeping with the principles of international law and I so find."

11. *Application of International Law*

11.1 Upon the basis of the facts recited in paragraph 2.1 above, there can be no doubt that in executing the agreement between Sandline and PNG, the Deputy Prime Minister, Mr Haiveta, purported to act on behalf of PNG. Not only did he purport to exercise the authority with which he was invested by his official position, but he did so after negotiations involving the Prime Minister and the Minister for Defence and with the approval of the National Executive Council and the National Security Council. No question of illegality was raised with Sandline. In these circumstances, for the reasons given above, a valid contract was concluded between Sandline and PNG, notwithstanding

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[14] 5 *Ann Dig* 179.

[15] 83 *ILR* 500.

any failure to observe the constitutional and other statutory provisions upon which PNG relies to establish the illegality or unlawfulness of the agreement or lack of capacity to enter into it. Any such illegality or unlawfulness or lack of capacity arose, if it arose at all, under the internal laws of PNG and not under international law which, for the purpose of determining the validity of a contract, disregards the internal laws of a contracting State. The agreement was not illegal or unlawful under international law or under any established principle of public policy. A political decision having been made by PNG to enter into it, its execution by a person with apparent authority to bind the State gave rise to a valid contract in the eyes of international law.

11.2 In addition, PNG participated in the performance of the contract before the events of 16 March 1997. It paid the first instalment of US $18 million due under the terms of the contract. It facilitated the entry of Sandline personnel and equipment into PNG for the purpose of carrying out the contract. Even after the events of 16 March 1997, PNG affirmed rather than denied the existence of the contract by alleging that it had been frustrated by those and later events and counterclaiming on that basis. It was not until late in these proceedings that PNG abandoned the defence of frustration and raised the defence of illegality or unlawfulness. Although it is strictly unnecessary to do so, in the light of the matters referred to in paragraph 10.3 above, the Tribunal expresses the view that, in the events which occurred, PNG is precluded from denying the validity of its agreement with Sandline.

12. *Conclusion*

The Tribunal rejects the defence of illegality or unlawfulness raised by PNG. In the end that is the only defence raised, and it follows from its rejection that PNG is liable to Sandline for its failure to perform the terms of the contract.

13. *The Consequences*

13.1 As mentioned in paragraph 7 above, in the course of the hearing in London the parties made submissions and reached certain agreements about the form and contents of the Tribunal's Award, depending on its conclusions on liability. The position in that regard, in the light of the conclusion in paragraph 12 above, is now as follows:

(a) It was agreed that if Sandline succeeded on liability, then the second payment of US $18 million became due and payable under the Agreement and is recoverable by Sandline as a debt, without raising any question of quantum. The Tribunal agrees with this conclusion. In a subsequent written communication PNG appeared to wish to qualify this agreement by contending that an order for the payment of this second instalment would constitute an order for the specific performance of an illegal contract. However, the Tribunal has already rejected the defence of illegality and also disagrees with the submission that an order for payment of this sum is open to any other objection.

(b) The parties agreed that, in the discretion of the Tribunal, any sum awarded should carry interest at the rate of 8%.

(c) It was agreed that Sandline's additional claim for US $1.4 million on account of equipment storage charges, and PNG's defences to this claim, would require further submissions and a further hearing before this aspect could be dealt with in a Final Award.

(d) PNG having withdrawn its cross-claim for the US $18 million already paid as an issue in this arbitration, there is nothing for the Tribunal to do in that regard. Sandline reserved its position in all respects in the event that PNG should hereafter seek to recover this sum in other proceedings.

(e) It was agreed that, in the event of PNG failing in its defence of illegality, and having already abandoned its first defence of frustration, so that Sandline succeed on liability, Sandline would be entitled to all the costs of the arbitration to date, and the Tribunal agrees with this conclusion. As regards the quantification of such costs, the parties agreed to exchange written submissions and that the amount of any costs awarded could accordingly not be dealt with in this Interim Award. However, it was impliedly accepted by PNG, in the Tribunal's view clearly rightly, that in the event of Sandline succeeding on liability, Sandline would be entitled to the release of the sum of £40,000 referred to in paragraph 5.2 above.

(f) It was agreed that any Award should be deemed to have been issued in Cairns, the seat of the arbitration, without the Tribunal having to meet there to sign it.

13.2 The Tribunal accordingly makes its Interim Award in the light of the foregoing matters.

14. *The Award*

1 Sandline are entitled to recover from PNG the sum of US $18,000,000 together with interest at the rate of 8% from 9 March 1997 to the date of this Interim Award and thereafter at the same rate of 8% on the foregoing total amount of principal and interest until payment.

2 Sandline are entitled to their reasonable costs of the arbitration to date, in a sum to be determined by the Tribunal hereafter, if not agreed between the parties.

3 Sandline are entitled to the immediate release to them of the sum of £40,000 referred to above.

4 PNG must bear the costs of the arbitration to date. PNG must accordingly repay to Sandline on demand the full amount of the contributions paid by Sandline to the fees and expenses of the Tribunal and to any other common expenses such as the hire of rooms, the cost of transcripts, etc. Any remaining dispute in this regard will be resolved by the Tribunal hereafter.

5 All other matters in dispute are to stand over for a Final Award, if not agreed between the parties.

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3 Full details not available – cited by Kirry, op cit, at 384,385.

4 As above - Kirry, op cit, at 376.

5 As above – Kirry, ibid.

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[6] Full details not available – cited by Friedland, op cit, at 111, op cit.

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