The New Lex Mercatoria: The First Twenty-five Years

"FEW readers are likely to welcome an article on the lex mercatoria by an English lawyer. The common lawyer will not look kindly on an addition to the extensive literature on what he may be tempted to regard as a non-subject, having no contact with reality save through the medium of a handful of awards which could well have been rationalised more convincingly in terms of established legal principles. Conversely, a scholar nurtured in other disciplines may well anticipate yet another reactionary response to any doctrine lying outside the tradition of Anglo-Saxon jurisprudence. Perhaps there is a middle course. The auspicious occasion which this volume is designed to commemorate deserves better than a reaction by rote or a routine polemic. The lex mercatoria has sufficient intellectual credentials to merit serious study, and yet is not so generally accepted as to escape the sceptical eye. It therefore seems appropriate to try a fresh approach. Commercial arbitration exists for one purpose only: to serve the commercial man. If it fails in this, it is unworthy of serious study. The commercial man is a conspicuous absentee from the writings on the leer mercatoria, and so indeed is his adviser. One may therefore approach the subject from an angle rather different from the one usually chosen. Imagine that a practical lawyer is retained to advise a client who has become involved in a dispute which may lead to an international arbitration. The lawyer knows enough about modern theory to have heard of the lex mercatoria, and can envisage the possibility that if the matter does come to arbitration, he may find that the arbitrators, whose identities are at present unknown, may at least consider the application of the lex. A conscientious practitioner, he recognises the need to warn his client of this, and seeks to anticipate, and prepare himself to answer, the questions likely to be asked by a businessman who encounters the doctrine for the first time. These are likely to be on the following lines. What is the lex mercatoria? What kind of law is it? When does it apply? Does it enable the arbitrator to decide in equity, according to his own inclinations? How does the lex mercatoria relate to national law? What are its sources? How are its rules to be ascertained? What are the rules, when so ascertained? We may follow the adviser in his search for answers to these questions, and conclude by asking as he must surely ask himself - how the lex mercatoria stands today, and what its prospects are for the future.

I. WHAT IS THE LEX MERCATORIA?

Although the concept of a new lex mercatoria had been foreshadowed in earlier writings, systematic discussion of the concept first began to flower in the early 1960., under the stimulus of the London Conference on the Sources of International Trade in 1962, hence the title of the present essay. There followed several important treatises, including influential discussions by Professor Berthold Goldman and Professor C. M. Schmitthoff. The proposals have not by any means passed unchallenged, and a lively debate has continued to the present day.

A useful starting-point would be a definition. Unfortunately, there appears to be none which accommodates all opinions as to the nature of the doctrine. The same turn of phrase means different things to different scholars. The following may
however serve to give the flavour;

A set of general principles, and customary rules spontaneously referred to or elaborated in the framework of international trade, without reference to a particular national system of laws.\(^6\)

A single autonomous body of law created by the international business community.\(^7\)

This phenomenon of uniform rules serving uniform needs of international business and economic co-operation is today commonly labelled *lex mercatoria*.\(^8\)

The customs of the business Community may combine all general principles of law to create a system of commercial self-determination.\(^9\)

... un droit 'transnational', réceptacle des principes communs aux droit nationaux, mais creuset aussi des règles spécifiques qu'appelle le commerce international.\(^10\)

Also, from a rather less enthusiastic hand:

... an anational *lex mercatoria* or ...hybrid legal system finding its sources both in national and international law and in the vaguely defined region of general to principles of law called “Transnational Law”.\(^11\)

Notwithstanding the absence of any definition commanding general acceptance which is at the same time sufficiently detailed to serve as the focus of examination, it is possible to stare certain propositions which appear to reflect the majority of opinion.

In the first place, the *lex mercatoria* is "anational".\(^12\) This concept has two facets. First, the rules governing an international commercial contract are not, at least in the absence of art express choice of law, directly derived from any one national body of substantive law. Second, the rules of the *lex mercatoria* have a normative value which is independent of any one national legal system.\(^13\) The *lex mercatoria* constitutes an autonomous legal order.

A clear recognition of the anational character of the *lex mercatoria* enables a number of misconceptions to be avoided. Thus, the fostering of the *lex mercatoria* has nothing to do with the harmonisation of international trade law. The aim of the latter is to minimise the differences between the laws of individual nations, so as to provide a stable and uniform basis for commerce. To the mercatorist the laws of individual states are irrelevant, save as a quarry from which to draw the raw materials for generalised rules.

Again, the *lex mercatoria* resembles in name alone the common body of doctrine the reception of which into various national laws has ensured that in matters of commerce there is a strong family resemblance between laws of developed trading States. Cross-fertilisation between legal systems has been a powerful instrument for more than two centuries in the elaboration and refinement of national laws. So too has been the adoption of propositions and concepts advanced by influential commentators who command an international breadth of learning. Equally important has been the recognition of trade practices acknowledged as binding, regardless of national frontiers. But the national judge who draws upon this common reservoir of rules and notions does so for the purpose of better fitting his own law to the task in hand, not as a means of applying some other body of rules in preference to the governing national law.\(^14\) Lord Mansfield, whose memory is not infrequently summoned to provide common-law credentials for the new doctrine,\(^15\) did undoubtedly speak of the *lex mercatoria*, but I believe he would be astonished to learn that while availing himself of the experience of his special jury and the wisdom of the learned expositors, he was doing anything other than making sure that the English law which he applied to the contract was serviceable, up to date and intellectually sound. The idea that, sitting as he was in the court of King's Bench, it was his duty to set on one side the King's law, and to apply a law which was not the law of any nation, would have been quite foreign to his mind.\(^16\)

It is convenient at this stage to mention another misconception: namely that the *lex mercatoria* is in some way connected with, or a reflection of, the notion of transnational arbitration. The latter \(^{17}\) posits that there exists a category of arbitration
which is, or at least ought to be, detached from the procedural laws of the country where the arbitration takes place, or indeed of any other country, excepting only, in some limited degree, the law of the country where the award is sought to be executed. The subject-matter of the transnational doctrine is thus quite different from that of the lex. So too are its theoretical foundations. Not even life most enthusiastic transnationalist could claim that international commercial arbitration is now wholly distinct from national arbitration laws, or that it would be practical to sever all links with such laws, since the arbitral

process does from time to time need the help of the courts. The proponents simply assert that the links should be no greater than are strictly necessary to ensure that, through the coercive powers of the courts, a party who wilfully fails to honour the letter and spirit of his agreement to arbitrate can be brought into line. The theory of transnational arbitration is essentially a statement of practical policy.

The concept of the lex mercatoria is quite different. It is not the positing of an ideal which all concerned should unite to bring about. Of course it is desirable that the lee mercatoria should be developed and promulgated. Nevertheless, independently of any such endeavour, in the eyes of the mercatorists the lex mercatoria simply exists. It springs up spontaneously, in the soil of international trade. It is conceived to be a growth, not a creation.

Thus the debate on transnationalism is about whether it can and should be brought about. By contrast, the debate on the lex mercatoria is about whether it can and does exist as a viable system. A mercatorist need not be a transnationalist. There are, however, two possible points of contact. In the first place, the premise of the transnationalist theory is that, although an international commercial arbitration must in a physical sense take place somewhere, in the legal sense it takes place nowhere. It therefore cannot have a lex fori, and so cannot be the subject of any national system of conflict of laws, such as would ordinarily be applied as part of the lex fori. This is an interesting idea, which may be said to be reflected in practice: for many practitioners would readily acknowledge that in the small minority of cases where it makes the least difference what law is applied to the substance of the dispute (for most disputes turn on the facts and on the words of the contract), the arbitrators frequently abstain from referring themselves explicitly to the conflicts rules of the country in which they happen to be sitting, but rather proceed to an intuitive choice of the proper law. Whether this is because they are transnationalists at heart, I venture to doubt. I think it more probable that since the conflicts rules of most developed nations are much the same, so far as concerns the choice of proper law, it is not usually worth the trouble of deciding whether to follow one rather than the other.

A more testing question would be whether there is a body of transnational conflicts law which governs matters such as status, capacity, consent, and rights in rein. But about this, the mercatorists can have nothing to say, since the function of the lex mercatoria is to expound the content of the rights and duties of the parties under a contract which is ex hypothesi valid as between them and them alone. Furthermore, in the present context the debate is academic, since the purpose of the conflict of laws is to enable the tribunal accurately to identify the national law which governs the contract. This is precisely antithetical to the premise of the lex mercatoria, which is that the arbitrator's first step is to reject any national law as the governing law.18 Admittedly, it would be possible to have a specialist conflicts system with only one role - namely, that all disputes concerning international trade should, when referred to arbitration, be regulated by the lex mercatoria. But this is not, I believe, the drift of the extensive literature on the topic.19

Another possible point of contact between the two theories lies in the fact that transnational law seeks to release tire substantive content of an award from the control of a local court. If put into practice, this will, it is said, enable the arbitrator to make a free choice of norms, unfettered by any national law, and it will thus facilitate the development of the lex mercatoria. This scarcely seems a convincing ground for assimilating the doctrines. Absence of any method of demonstrating that the arbitrator has done wrong does not justify the inference that he has done right, and the release of judicial control is at least as likely to encourage the arbitrator to apply no law at all,20 as to apply the lex mercatoria.21

One final misconception is that the application of the lex mercatoria is equivalent to a decision in `equity' according to the arbitrator's own personal ideas of justice. This understanding of the doctrine may be at the root of the dismay with which it is still greeted in many circles not only in common law
countries. It does, however, seem clear from the writings that the classical mercatorist position is to regard the *lex mercatoria* as a system of law; and not as an expedient for deciding according to 'non-law'. I will return to this point later.

I now turn to the second of the general propositions which emerge from the literature: namely, that the prime sources of the *lex mercatoria* are the principles of law common to trading nations and the usages of international trade. These merit separate consideration.

Although the essence of the *lex mercatoria* is its detachment from national legal systems, it is quite clear from the literature that some, at least, of its rules are to be ascertained by a process of distilling several national laws. The intellectual justification for this process is nowhere clearly described, but it must, I believe, be found in the idea that the rules of the *lex mercatoria* exist in *gremio legis* as a complete, albeit inexplicit, and evolving whole; that they are received, at least in part, into individual national laws or are reflected by them; and that by careful analysis the dross of the rigidities, impracticalities, and distinctions imposed by each individual national law can be purged away, leaving behind the pure gold of the underlying international legal order. This rationale seems neither more or less convincing than an English jurisprudential theory to which it bears some resemblance: that the common law is revealed to and by the courts, rather than developed by them.\(^2\)\(^2\) Quite apart from this, the concept of the *lex mercatoria* as being in part a distillation of national laws soon runs into serious practical difficulties. The proponents of the *lex mercatoria* claim it to be the law of the international business community: which must mean the law unanimously adopted by all countries engaged upon international commerce.\(^2\)\(^3\) Such a claim would have been sustainable two centuries ago. But the international business community is now immeasurably enlarged. What principles of trade law, apart from those which are so general as to be useless, are common to the legal systems of the members of such a community? How could the arbitrators or the advocates who appear before them, amass the necessary materials on the laws of, say, Brazil, China, the Soviet Union, Australia, Nigeria and Iraq? How could any tribunal, however cosmopolitan and polyglot, hope to understand the nuances of the multifarious legal systems?\(^2\)\(^4\) In published awards the arbitrators occasionally make large claims about the universality of principles, but these are rarely if ever substantiated by citation of sources. Equally if not more important is the question: How could any adviser hope to predict what a tribunal not yet constituted might make of such a task in the future?

Evidently oppressed by these difficulties, some proponents of the doctrine have somewhat drawn back from the concept of what may be termed a 'macro' *lex mercatoria*, and have suggested that the law may be one which is 'common to all w\(^\ldots\)\(^\ldots\)most of the states engaged in international trade.\(^\ldots\)\(^\ldots\)\(^\ldots\)\(^\ldots\) To some readers it may seem that this solution gets the worst of all worlds. It fatally compromises the appeal of the *lex mercatoria* as a lex universalis. It undermines the intellectual basis of the doctrine, so far at least as this is understood to lie in the presumed intent of the parties to the individual contract, for how can it plausibly be asserted that a party of nationality X has tacitly agreed to submit his relationship with a co-contractor to a generalised law which is inconsistent with the national law of state X? In practice, moreover, the idea seems quite unworkable. If there are two intellectually respectable and firmly established doctrines on a particular issue, one adopted by one group of legal systems and one by another - as does of course, quite often occur, even within the modest horizons of the Western European and common-law systems - how is the arbitrator to know which is adopted by the majority of States? Surely not by arithmetic. When the generality of trading nations enters into the calculation, it may verge on the absurd. There may be instances in which, if the data were meticulously examined, a number of solutions would be disclosed, all sustainable and none commanding a majority. True it is that one or two of the very few reported awards have claimed to apply rules of law adopted by the majority of States; but I suggest that in reality this meant the majority of states with whose laws the tribunal was familiar. This cannot be the basis of a workman-like framework for the conduct of business relations.

Perhaps in response to these pressures, another concept has evolved. By contrast with the world-wide horizons of the orthodox doctrine, there has emerged the idea of what may be called a 'micro' *lex mercatoria*. This is a law merchant generated with specific reference to the individual contract. On this basis, the *lex mercatoria* need not be the same all over the world. The arbitrator will tend to confine his investigations to those legal systems which are connected with the subject matter of the dispute.\(^\ldots\)\(^\ldots\)\(^\ldots\)\(^\ldots\) Thus, the arbitrator will seek out 'au sein d\'un petit groupe de systems juridiques', an individual solution to the problem under scrutiny thereby arriving at a partial internationalisation of private law.\(^\ldots\)\(^\ldots\)\(^\ldots\)\(^\ldots\) Looked at in terms of the individual dispute, this does provide the
arbitrator and the adviser with a task which is more practicable to fulfill. But what precisely is the nature of this variety of lex? Is it to be supposed that there exists a constellation of pares-laws, Franca-Belgian, Anglo-Dutch, Italo-Hispano-Korean, and so on, from which the arbitrator chooses the one most appropriate to the individual dispute? The idea is surely fanciful. The only alternative is that a law is newly minted by the arbitrator on each occasion, with every contract the subject of its own individual proper law. Whatever the merits of this concept, it appears to have no point of contact with the classical lex mercatoria, conceived as a universal and pervasive "arrière-plan" underlying every arbitral decision in the field of international commerce.

We may now turn to the second of the primary sources: namely, international trade usage. Here again, there is a risk of imprecision through the use of the same label to denote different concepts. At its widest, usage is simply a practice which is generally followed. So understood it cannot be a source of law or of individual legal rights. It can be such only if the practice is generally followed because commercial men regard themselves as bound to follow it in the absence of express stipulation to the contrary. Nobody could deny that usage in this sense can be an important element in the assessment by a tribunal of the rights and duties created by the contract, either because in a codified or in explicit form it is tacitly incorporated into the contract, or because it has been received into the relevant national law. But there is nothing special about international trade in this respect, nor anything special about arbitration. Any worthwhile national court ought to be capable of taking usage into account, without the need to accord to usage the status of a prime element in self-contained system of law.

There is, however, a different form of usage to which some of the proponents have had recourse, namely, the practice of contracting within various trades, on standard forms of contract. The mechanism whereby these terms become part of a standing body of law is rarely spelt out. One suggestion is that they express the sense of justice of those who draft and enter into them. I confess to some reservations about this proposition. Often, one party to a standard form contract adopts it because the other party gives him no choice. More important, the form does not, it seems to me, reflect the ideas of anybody as to the justice of the transaction, if indeed this concept has any meaning in the field of commercial transactions negotiated between parties on an equal footing. Rather, the form is designed to serve as a convenient peg on which the parties can hang the specifically negotiated terms, without having to work out all the details of the transaction from scratch. Experienced traders are aware of the general financial balance of the transaction contemplated by the standard form, and know the way in which it distributes the commercial risks between the parties. With this in mind they can negotiate towards agreement on matters such as price, delivery date, insurance, demurrage, and so on. If the standard form is altered so as to throw more obligations or risks on to one of the parties, the negotiated terms will have to be adjusted to restore the balance. The second form will be neither more nor less 'just' than the first. It simply calls for a different assessment of the price in the widest sense of the term.

Furthermore, there are serious practical objections to the use of standard forms as a source of law. Quite apart from the fact that a single institution within a single trade may publish a repertoire of different and mutually inconsistent documents from which the contracting parties may choose the most suitable to reflect the balance of their bargain, there coexist in many trades a number of institutions, each offering its own standard form; and it is, of course, a commonplace that parties alter the standard forms to suit their own purposes. There is thus no guarantee of homogeneity even within a single trade. Moreover it may legitimately be asked why a participant in one trade should be supposed to have consented to have his contract governed by rules drawn from contract forms current in a quite different trade.

Finally, it must be confessed that the mechanism whereby the use of standard forms becomes a source of law is nowhere clearly explained. The simple repetition of contracts on the same terms is as consistent with the exercise of freedom of contract as with subordination to a system of binding norms indeed, far more so, since if the parties to a commodity transaction do not wish to bind themselves to, say, the GAFTA Contract Form No. 100, there is no legal or other institution which can compel them to do so. Moreover, the repetition of transactions in the same form could at most create a group of norms peculiar to the individual trade, thereby creating a network of para-legal systems. This is inconsistent with the theoretical premises of the lex mercatoria, which is that it springs spontaneously from the structure of international commerce - and this is plainly regarded as an indivisible whole.

II. WHAT KIND OF LAW IS THE LEX MERCATORIA?
This question cannot fruitfully be debated without some sort of common ground about what is meant by a law, and what is meant by the *lex mercatoria*. Since philosophers of law cannot agree about the one, and students of international law cannot agree about the other, the discussion soon becomes clouded. Interesting as it is, the businessman would be unlikely to linger over the question, and lack of space compels the present author to follow suit. As Jenks pointed out, the question whether the general principles of law, conceived as a system, can serve as the proper law of a contract depends, not on any preconceived notion of what constitutes a legal system, but on whether they can fulfil satisfactorily in practice the function of a proper law, and are in fact used for that purpose. To this the present author would add the rider that the principles applied by the arbitrator must be such that they will be recognised by courts as founding a valid award, for an unenforceable award is not an instrument of law or of commerce. The reader must form his own opinion on the question, but even the most ardent supporter would hesitate to say that the *lex mercatoria* is yet ready to satisfy these criteria in full.

One facet of the problem might however interest the businessman and his adviser. If the transaction is governed by an international agreement or a standard form of rules which require the arbitrator to choose the `law' which he deems applicable to the substance of the dispute, is he thereby enabled to apply the *lex mercatoria* to the exclusion of any national law? For example, is the *lex* a permissible choice under Article 33(1) of the UNCITRAL Model Arbitration Rules or Article 13(3) of the ICC Arbitration Rules of Article 42 of the World Bank Convention or Article 7 of the Geneva Convention or Article 28(2) of the UNCITRAL Model Law? The point does not admit of much development, but I suggest that the answer must surely be, no. Again, although there is room for difference of opinion, the same answer suggests itself where there is a reference to `law' in the contract itself, or in the submission to arbitration.

The juridicial status of the *lex mercatoria* has another, more troubling aspect. Let it be assumed that whether or not the *lex* qualifies as a law, it has sufficient solidity to be capable in appropriate circumstances of controlling the rights of the parties; then the question must be asked, from where does its normative power arise? Here, I believe, there are two deep-rooted divisions of opinion among the proponents, quite distinct from the differences of emphasis already noted as to the respective weight to be given to custom and the common core of national laws.

The first concerns the method by which the *lex* comes to govern an individual transaction. One concept is that the *lex* is a standing body of legal norms, which automatically applies *ipso jure* to every transaction within its purview, unless expressly excluded. The other is that the *lex* provides, so to speak, a repertoire of rules available to those parties who, expressly or by implication, choose to incorporate them into their dealings, and who, by the same token, choose to detach their contracts from the national law to which they would otherwise be subject. There is really no common ground between these two perceptions of the *lex mercatoria*.

The second discontinuity in mercatorist theory concerns the role of arbitration and the arbitrator. One view is that the *lex* is a constant presence, applicable or not according to the circumstances of the individual transaction. If it applies at all, it does so from the inception of the bargain, and the sole function of the arbitrator is to uncover it and apply it to the dispute in hand. The alternative opinion is that the *lex mercatoria* reflects an economic order of which international arbitration is an indispensable element. In making his award, the arbitrator does not simply expound a *lex mercatoria* which is already there, albeit inchoate; but rather creates new rules, which he then applies retrospectively to the original bargain. Yet further away from the first concept is the notion that, in the absence of established norms, the arbitrator exercises a creative function, acting as a social engineer.

It is plain that these appreciations of the *lex mercatoria* have little in common. This may be illustrated by assuming that an international arbitrator is faced with a previous award which decided precisely the question of law which is brought before him. If the arbitrator's function is simply that of an exponent, then the second arbitrator need do no more than pay appropriate respect to the reasons of his colleague, without being obliged to arrive at the same decision. If he thinks fit, he is at liberty to hold that his predecessor misunderstood the *lex mercatoria*. Again, at the other extreme, if the first arbitrator has exercised a creative function as a social engineer, his successor can fairly regard him as no more than a part of the self-regulating mechanism of the contract under which he acted, and can thus feel free to exercise the same function, in a different sense, under his own contract. But if the intermediate theory is correct, an award which enunciates a new rule thereby adds to the corpus;
arid since the lex is conceived to be a binding law, the subsequent arbitrator must apply it, whether he agrees with the conclusion or not.

These examples may serve to explain why the present author has been driven to the conclusion, after a study of the literature, that the theoretical foundation of the doctrine has not yet been made explicit. Thus far, the number of awards in which the arbitrator has set out to apply the lex mercatoria has been so small that the theoretical problems have been of little practical significance. But if the lex mercatoria is to assume the role in a world which its proponents claim for it, there must be a clear consensus about what the label actually means; for otherwise there will be a risk of that inconsistency and uncertainty which is fatal to the efficient conduct of commerce.

III. WHEN DOES THE LEX MERCATORIA APPLY?

Given the weight of analysis to which the lex mercatoria has been subjected, it is surprising how little has been done to identify the criteria which distinguish those transactions which are governed by it from those which are not.

One matter is treated by commentators as axiomatic: namely, that an express agreement to apply the lex mercatoria will and must be honoured by the tribunal, as well as the parties, and that such an agreement may take the form of a reference to, say, the general principles of law recognised by civilised nations or to the usages of international commerce. In the absence of express consent, it is generally held that the arbitrator should proceed by three stages, asking himself first whether the application of any national system is appropriate; then, if not, whether he should proceed by amiable composition or by the application of anational rules; and finally, if the latter, what anational rules exist and are relevant to the dispute. Various groups of factors have been regarded as relevant to this process.

The first group concerns the parties themselves. Clearly, the fact of their having different nationalities is important, and perhaps indispensable. Their character is also material, since it is easier to hold that the lex mercatoria, or that variant of it known as 'the general principles of law', is relevant if one of the parties is a sovereign State or an entity under immediate State control, especially in those cases where the proper law of the contract, according to the orthodox conflicts rules, would be the law of the State. It is also said to be significant if one of the parties has a 'transnational' character, apparently because such parties are to be regarded as existing in free space, detached from national allegiances, and hence especially apt for subjection to a system of law which is similarly detached.

Other indicators relate to the nature of the transactions. It is said to be significant, and perhaps conclusive, if the transaction has an 'international character'. Apart from the obvious rose where the parties are of different nationalities, it is not clear what this expression implies. Is a contract between private parties of the same nationality for the carriage of goods from one country to another or for the performance of services abroad of an international character sufficient to make the lex mercatoria applicable in a case where, according to ordinary principles, the law of one of the two countries would be the governing law? The literature does not develop the question.

The subject-matter of the transaction may also be relevant. It is plain that many authors instinctively picture international arbitration as concerned with disputes under complex contracts, negotiated ad hoc, for the execution of major engineering or similar projects over a substantial period of time. This is perhaps natural, since the attention of mercatorists has tended to focus on awards springing from ICC arbitrations or from ad hoc arbitrations, of considerable size and duration. These arbitrations, which are not typical of international commercial arbitration as a whole, are more readily accommodated within the concept of an isolated autonomous legal system than the far more numerous arbitrations arising front everyday informal commercial transactions. Yet it seems that even the latter are regarded as being subject to the lex; for although the much discussed ICC Award No. 2291, which concerned just such a transaction, has been described as particularly ambitious as regards the manner of reasoning, there is no suggestion by the commentators that the tribunal should never have been thinking in terms of the lex mercatoria at all. This seems far removed from practical reality. Disputes concerning sale and transportation are being arbitrated by the thousand every year, and lute present author has never heard of any instance in which it has even been suggested, let alone decided, in any such arbitration held in the common-law world.
that in the absence of express provision the dispute should be referred to an anational system of law.

Another group of indicators relates to the terms of a contract. This is certainly understandable in so far as the application of tire *lex mercatoria* is taken to rest en express or implied consent; but it is less easy to comprehend when the law is said to apply because the transaction is effected within the matrix of the legal order constituted by international commerce, for the transaction either is, or is not, of a type falling into this category, and its terms as to jurisdiction and so on should be immaterial. Be that as it may, the presence of a clause of *amiable composition* is conceived to he material, for reasons which will he mentioned below; it has also been suggested in the literature that the inclusion of an arbitration clause or the choice of an international tribunal or of a clause referring disputes to an international arbitration centre are pointers towards the *lex mercatoria*. If this is right, then international arbitrators have been mistaking their functions, day in, day out, for many years.

Again, it has been suggested (that the absence of a choice of law clause is an indication that the parties wish to apply an anational system, apparently because it shows that the parties could not agree about which systems should govern. This striking proposition ignores the possibility that the choice of a national law was so obvious as not to be worth mentioning, or that the parties never thought about the matter at all. Moreover, even if the parties had in fact disagreed, there seems no warrant for inferring unanimity in favour of ruling out all potentially relevant national systems and substituting an anational system of which only the smallest minority of businessmen can ever have heard.

These are the factors which are said to be material to an arbitrator’s decision to set aside national law, to direct himself towards a system of law rather than a free equity, and to find that system in the *lex mercatoria*. Unfortunately, it is not explained in the literature how he is to perform this operation, and in particular, how much weight is to be attached to the individual factors. The mercatorists can fairly respond that there is no mechanical process for arriving, by way of the conventional conflicts of laws, at a choice of the governing law; and that indubitably a decision on this issue may be finely balanced and susceptible to differing conclusions. Nevertheless, the general nature of the exercise to be performed is comprehended well enough. Looking for the ‘closest connection’, or some local variant, may be difficult to perform but it is not difficult to understand. By contrast, the process for deciding when and when not to apply the *lex mercatoria* seems never to have been clearly spelt out.

Two more points are important. The first concerns the application of the *lex mercatoria* in cases where there is no arbitration clause and The dispute necessarily falls to be decided by a national court. It appears to be taken for granted that an express choice of the lex mercatoria would be effective in such a case. This may be overoptimistic, for it cannot he assumed that a national judge will be permitted by local law to enforce such a choice; or will even know how to do so. There appears to be little trace in the literature of attempts to apply the *lex* in national courts.

If this does, however, happen the question will arise whether the national judge ought to apply the *lex mercatoria* to the exclusion of whatever national law would otherwise be regarded as the proper law, even in the absence of an express choice, in those instances where it would have been applicable if the contract had contained an arbitration clause. (By this I mean the *lex mercatoria* applied directly as a body of anational law, rather than a series of trade customs carried into a contract via the proper law.) It is disappointing that this problem has been so little addressed for it discloses the existence of a fundamental uncertainty about the theoretical underpinnings of the doctrine. If application

of the *lex* to the individual contract is seen as a matter of implied consent, then the relative importance of the arbitration clause becomes crucial, for if it is conclusive or near conclusive evidence of a wish to apply the *lex*, then it might be said that its absence is equally significant; so that instances in which a national court should give effect to the *lex* must be non-existent or at best rare. Again, if the *lex* applies independently of consent to all transactions falling within its purview, one must ask whether a contract without an arbitration clause is within its purview. This in turn raises the question whether the left is generated by, and is an integral and necessary part of, the societas mercatorium; or whether it is generated by, and is an integral and necessary part of, international commercial arbitration: two entirely different matters. These uncertainties will have to be resolved before the *lex* can present itself convincingly to the business community, which can hardly be expected to accept it as a substitute for the existing regime in the absence of an explicit formulation of precisely what it is.

Finally, it must be noted that the *lex mercatoria* has not yet laid claim to the whole territory of potential disputes arising from international commerce. Thus: (i) there appears to be no instance in which the *lex* has been invoked in a case of
pure delict: (ii) the lex has rarely been applied where the issues are those of consent, fraud in the making of a contract, and so on; (iii) the lex has not, as far as the present author is aware, ever been credited in the literature with a power to create rights in rem, valid as against third parties - for example, by way of a transfer of title of corporeal assets, or pledge, or the creation of a monopoly such as patent or copyright. This is explicable, and indeed inevitable, if the lex is regarded as applicable only by express or implied consent, but is harder to understand if it is merely a reflection of the international commercial organism. Moreover, once it is accepted that the lex may on occasion have to be applied to some aspects of a dispute, whereas national law is applied to others, the practical attractions seem less apparent.

IV. DOES THE LEX MERCATORIA EMPOWER THE ARBITRATOR TO DECIDE IN EQUITY?

Much of the unease about the lex mercatoria stems from the idea that it frees the arbitrator to apply his own unfettered standards of justice to the individual case. The fact that this misconception is so widespread is due in part of the ambivalence in much of the literature about the relationship between the lex mercatoria and the concept of amiable composition, a concept which is itself hard for the common lawyer to grasp. Nevertheless, a misconception it undoubtedly is, at least by classical mercatorist standards. The lex mercatoria is a lex, albeit not yet perfected. It creates norms which an arbitrator must seek out and obey in every case to which the lex applies. Whether the reason for its application is understood to be an express or implied agreement between the parties, or the concept that it forms the essential juridical context of the bargain, there is no room here for the arbitrator to impose his own ideas, unless of course they happen to coincide with the rules of the lex mercatoria: for if he does so, he falsifies the transaction. Naturally, everyone hopes that the lex mercatoria will in every case yield a solution which will seem fair to all. But even if this expectation is disappointed, the lex mercatoria must still prevail; otherwise it would not be a law. Thus, since the prime maxim of the lex mercatoria is that pacta sunt servanda; an arbitrator who smooths the corners of a contract which seem to him too sharp is not complying with his mandate.

More difficult is the reciprocal relationship between the two concepts. It has been said that an agreement to make the arbitrator an amiable compositeur enables, even if it does not require, the arbitrator to take note of the lex mercatoria. To an outsider, this seems strange. The essence of amiable composition is to dispense the arbitrator from the duty of enforcing any system of law. Yet the lex mercatoria is a system of law. Why should an agreement to amiable composition summon up a reference to lex mercatoria any more than to any other developed system of commercial law? The literature gives no convincing answer.

Another idea is that the repetition of decisions in equity will generate rules apt to be applied even by an arbitrator who is not authorised to act as an amiable compositeur. In practice, this seems far distant; as scrutiny of the reported awards will disclose. But the theory is also difficult. How can decisions by arbitrators who ex hypothesi are released from the duty of applying the law ever yield a system of law which all arbitrators are bound by?

V. WHAT IS THE RELATION BETWEEN THE LEX MERCATORIA AND NATIONAL LAW?

A hypothetical client is likely to ask how a conflict between the lex mercatoria and any national law which might otherwise have been relevant ought to be reconciled. H is adviser would probably reply that the question has two aspects. First, what solution should the conscientious arbitrator adopt? Second, what is likely to be the attitude of the courts claiming jurisdiction over the matter namely, the courts of the countries in which the arbitration takes place and the country in which enforcement of the award is sought?

On the first aspect, the bluntest question which the client may pose is this: If the contract expressly stipulates a choice of governing law, and if the arbitrator is not an amiable compositeur, can the arbitrator properly apply the lex mercatoria in preference to the chosen law? The answer must surely be an equally blunt no. The arbitrator is mandated to decide the dispute in accordance with the contract; and the contract includes an agreement to abide by the denominated law. An
arbitrator who decides according to some other law, whether anational or otherwise, presumes to rewrite the bargain. He has no right to do this. However good his motives, he does a disservice to the parties and to the institution of international arbitration.

Most complicated is the situation where the parties have expressly chosen to apply both a national law and some variety of ‘general principles of law.’ This does happen on occasion, particularly where one party is a State enterprise. In practice, this rarely creates problems, because most often either the State law or the lex mercatoria are silent on the crucial question, or the answers given by the two laws happen to coincide. Occasionally, however, a hierarchy must be established. Here, the literature offers no clear solution, and there appears to be no reported award where the arbitrators have been forced to make a choice. There is a similar lack of authority in the converse situation, where the contract contains no express reference to a national law or to the lex mercatoria. This is not surprising. Classical mercatorist doctrine requires the arbitrator to reject the choice of a national law before proceeding to choose the national law (see page 96). A conflict between the two should not arise. This theoretical conclusion appears to be reflected in practice. Those few awards in which the topic is touched upon seem to avoid discussion of conflicts between the lex and national laws, but rather tend to call up concordant national laws as reassurance that the rules of the anational laws have been correctly stated.

There has, however, been some degree of discussion about the relationship between the lex mercatoria and national rules of ordre public and between the lex and what has been called international ordre public. Regrettably, space does not permit a discussion of this interesting and elusive topic.

The second question concerns the likely reaction of national courts to an overtly anational award. A study of this question, which is difficult enough even when expressed in terms of a single national law, is far beyond the scope of the present essay, and indeed never appears to have been attempted. The question seems scarcely to have arisen in practice but if it had done so, the attention currently given to the world-wide claims of the lex would hardly have allowed it to be overlooked. It is, however, impossible to part from the subject without mentioning, much more briefly than the author would have wished, three awards where the issue has come to the surface.

The first was rendered in the arbitration Soc. Fougerolle a. Banque de Proche Orient. Arbitrators were authorised to decide what law was to be applied. Without the possibility being mentioned by or to the parties, the tribunal decided the dispute according to the principles generally applicable in international commerce. The Cour de Cassation in France rejected an attack on the award, but it is not clear from the economical reasons given by the court whether the decision was founded on the principles of contradiction or on the lex mercatoria itself. As a commentator has suggested, it may be unsafe to draw too many conclusions from it.

The second instance is the much debated case of Pabalk Ticaret v. Ugilor/ Norsolor The arbitrators found it difficult to choose between two national laws, and therefore elected to choose neither, applying the rule of the lex mercatoria which requires the parties to act in good faith in the execution of the contract. Holding on the facts that one party had abused its position of strength in a manner which had led to the breakdown of the agreement, they awarded damages to the other.

The award came under repeated scrutiny in the courts of two countries. In Austria, where the award had been made, the Oberster Gerichtshof confined itself to the question of whether the award should be annulled on one of the grounds set out exhaustively in ZPO, Article 595, of which only paragraphs five and six were relied upon. These dealt respectively with situations in which a tribunal had entered upon matters beyond those confided to it, and those in which an award violated mandatory provisions of law. As to the first, the court held that an award resulting from an unauthorised application of equity was not an award on matters outside the powers of the tribunal. As to the second, there was no evidence that the application of equity contradicted any statutory imperative of the two laws in question. Thus, it appears that the decision was not an endorsement of the lex mercatoria so much as a recognition of a court's limited powers where a tribunal's reasoning is under attack.
In France the successful party sought *exequatur*. It was first granted, then denied, and later the denial was made the subject of cassation, each decision following the fortunes of the proceedings in the Austrian courts. The decision of the Cour de Cassation certainly does lend support to the mercatorists, to the extent that the court did not repudiate the notion of the *lex mercatoria*, which would have furnished a short answer to the problem. Whether it amounts to a vindication of the *lex*, as has been claimed, is an altogether different matter; and it may be noted that Professor Goldman, amongst others, has expressed the opinion that it does not go so far. 75

The third decision, arising from a dispute between *Deutsche Schachtbau und Tiefbaugesellschaft mbH* and *The Government of Ras al Khaimal*, will be welcomed by mercatorists, and seems likely to be the subject of extensive academic discussion. The circumstances were as follows.

An agreement relating to exploration for oil and gas was made between a government and a government oil company on the one hand, and a consortium of companies registered in various countries on the other, upon terms which included an ICC arbitration clause providing for the arbitration to be held in Geneva. Subsequently the government and the oil company declined to continue performance of the agreement, contending that it had been induced by misrepresentation. The dispute which then arose was submitted to arbitration. The government side took no part. In due course terms of reference were formulated, stating a number of issues for decision. The second was: 'What body or bodies of substantive law should be applied by the tribunal?' Ultimately, the arbitration was decided on the facts, the arbitrators holding that the alleged misrepresentation was not established and that there was no other ground for holding that the agreement was invalid. As the arbitrators themselves said in their award (IC C No- 3572) 'the choice of the law to be applied to the agreement is of little significance; if any, under the prevailing circumstances'. In spite of this the arbitrators went on to express a choice, presumably because they felt obliged to do so by the terms of reference. Rejecting the law of the state where the agreement was to be performed they held that internationally accepted principles of law governing contractual relations were 'the proper law'.

Understandable as it was, the election to include in the award a reference to international principles which had no bearing on the outcome of the dispute proved to be unfortunate, since the oil company relied upon the choice of these principles as a ground for resisting enforcement of the award in England, thus postponing the time when the sums awarded would be recovered.

When it was discovered that the oil company might have assets in England,

various proceedings took place, including in particular a summary application to the Commercial Court, to enforce the award in the same manner as a judgement. This was granted. Subsequently there was an application to the same court to set the order aside oil the grounds that it would be contrary to public policy for the court to grant enforcement, where the principles applied by the arbitrators were so uncertain. This application failed. The oil company appealed to the Court of Appeal, and failed again.

This is an important case for an English lawyer, as regards both the recognition by the court of a doctrine of *competenz* applicable under the *lex fori*, and also the application of a narrow view of English public policy. Tile significance so far as regards the *lex mercatoria* is, however, substantially less than might at first sight appear. The starting-point of the judgement was a decision that the agreement to arbitrate was governed by the law of Switzerland. Since the oil company did not participate in the arbitration, there had been no contest on the propriety of a choice of general principles under that law. The company had not sought to set the award aside in Switzerland, nor did it offer any evidence to contradict the expert evidence of Swiss law tendered by the claimants to the effect that the general principles were a valid choice under the ICC choice of law clause. Thus, the English court could accept that the decision to apply the general principles was a permissible performance of the arbitrators' mandate under the choice of law clause according to both the *lex fori* and the *lex causae*. Against this background there was nothing in English public policy to preclude enforcement of the award in England.

Thus far, the import of the decision is clear, and it must greatly hearten the mercatorists. The wider implications, so far as concerns English law, will require careful analysis. As an immediate reaction. the present author would venture the following very tentative observations. 75 b

(i) The case was not concerned with transnationalism. The claimant's evidence proceeded on the assumption that Swiss law was the *lex causae*. Nobody suggested that there was no national *lex causae*.

(ii) Although the judgement contains a discussion of two English decisions on the effect on a contract of including
various types of 'general principles' clauses, this was probably obiter, since (a) there was no such clause in the contract, (b) English law was neither the lex causae, the lex loci, nor the 'putative proper law', and (c) the issue had not been argued.

(iii) The judgement did not address the question whether, under English law, when a contract does not contain any explicit choice of the 'general principles' the arbitrators can validly purport to apply them. This extremely important question did not arise in the Court of Appeal, and could not have been decided without reference to certain reported cases, not cited in the judgment.

VI. WHAT ARE THE SOURCES OF THE LEX MERCATORIA?

It is, I believe, clear from a reading of the literature, that the proponents of the lex mercatoria do not wholly agree about the sources from which it is drawn, or about the relative importance of those sources which they regard as admissible. There is a wide gulf between those who look (for example) to sources such as standard form contracts and those who seek to distill the common features of national commercial law. Nevertheless, an adviser could not begin his task without first having an idea of the sources which the arbitrator might regard as relevant. For this purpose he could usefully have recourse to a list compiled by Professor O. Lando, noting, however, the caution added by that author that it is not possible to provide an exhaustive catalogue of all the elements of the law merchant. Reduced to its bare headings, this list is as follows:

A. Public International Law
B. Uniform Laws
C. The General Principles of Law
D. The Rules of International Organisations
E. Customs and usages
F. Standard Form Contracts
G. Reporting of Arbitral Awards

To this list one must evidently add the public policy of the country in which enforcement of the award is likely to be requested. Most of the items on this list are discussed elsewhere in this essay, but brief comments may be added about two of them. With regard to public international law, there is of course no question but that parties can expressly stipulate that their relationships shall be governed in whole or in part by public international law, and this does on occasion happen where one of the parties is a State or a State enterprise - the present author finds it hard to see why this fact should entail that the application of public international law in these instances should cause it to become part of an all-pervasive general law of commerce, applying between private parties even in the absence of express agreement; for the principles which are apposite to regulate the relationship between sovereigns are not a priori germane to the relationship between commercial persons or companies and in practice, the express incorporation of public international law into ordinary day-to-day trading contracts is, as far as the present author's experience extends, entirely unknown.

The inclusion of uniform laws - such as the 1980 Convention on the International Sale of Goods - in the list of sources is qualified by the suggestion that the arbitrator is bound to apply them only when the internal courts of those countries which are connected with the parties or the subject matter of the dispute would be obliged to apply them, although in other cases the uniform laws may act as a guide to the arbitrator. If this is so, we have here another example of a 'micro' lex mercatoria, particularised in relation to the individual transaction.

VII. WHAT ARE THE RULES OF THE LEX MERCATORIA?

Plainly, it would be of great practical importance to the hypothetical adviser to know whether in any published work, and particularly in any published award, the view had been expressed that a particular rule forms part of the lex mercatoria. Setting aside for a moment the difficulties of time and access to the literature which the adviser would be likely to encounter, it seems that he would be able to put together a list somewhat on the following lines, as representing
a tolerably complete account of the rules which are said to constitute the *lex mercatoria* in its present form.\textsuperscript{82}

1. A general principle that contracts should *prima facie* be enforced according to their terms: *pacta sunt servanda*\textsuperscript{83} The emphasis given to this maxim in the literature suggests that it is regarded, not so much as one of the rules of the *lex mercatoria*, but as the fundamental principle of the entire system.

2. The first general principle is qualified at least in respect of certain long term contracts, by an exception akin to *rebus sic stantibus*.\textsuperscript{84} The interaction of the principle and the exception has yet to be fully worked out.

3. The first general principle may also be subject to the concept of *abus de droit*,\textsuperscript{85} and to a rule that unfair and unconscionable contracts and clauses should not be enforced.\textsuperscript{86}

4. There may be a doctrine of *culpa in contrahendo*.\textsuperscript{87}

5. A contract should be performed in good faith.\textsuperscript{88}

6.

**Referring Principles:**

- I.1.1 - Good faith and fair dealing in international trade
- II.2 - Agent acting on behalf of group of companies
- III.1 - Set-off
- IV.1.2 - Sanctity of contracts
- IV.2.2 - Silence by offeree
- IV.2.3 - No repudiation of contractual consent by state party
- IV.5.3 - Interpretation in favor of effectiveness of contract
- IV.6.7 - Duty to renegotiate
- IV.7.1 - Invalidity of contract that violates good morals (*<em>boni mores</em>*)
- IV.7.2 - Invalidity of contract due to bribery
- IV.8.1 - Principle of pre-contractual liability
- VI.1 - Termination of contract in case of fundamental non-performance
- VII.2 - Principle of foreseeability of loss
- VII.4 - Duty to mitigate
- VIII.1 - Definition
- XIII.3.9 - Waiver of right to object