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GENERAL PRINCIPLES OF LAW IN INTERNATIONAL COMMERCIAL ARBITRATION

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GENERAL PRINCIPLES OF LAW IN INTERNATIONAL COMMERCIAL ARBITRATION

International arbitral rules generally allow parties to an agreement containing an arbitration clause to choose the substantive law that will govern disputes. Although the parties may choose the law of a particular jurisdiction, they often specify that “general principles of law” apply. Sometimes an inability to agree on any other law motivates the choice of general principles; sometimes the parties believe the choice will ensure neutral outcomes. In either case, however, the benefits of choosing a neutral forum are reduced because of substantial uncertainty about the content of these general principles.

This Note seeks to reduce this uncertainty by restating general principles of law as applied in actual international commercial disputes and agreed upon by scholars, international organizations, and sovereign states. Part I frames the problem by explaining the various contexts in which parties choose the substantive law to govern their agreements in case of arbitration. Part II then discusses the factors parties typically consider in making their choice, the rules that govern this choice, and the reasons that parties often choose general principles of law. Finally, Part III illustrates the mariner in which such principles are determined and sets forth seven principles frequently used to decide international commercial arbitrations. The heightened certainty resulting from the derivation of such principles, whether in this Note or in future works that continue the endeavor, may increase reliance on international arbitration as an efficient means of resolving investment and trade disputes.

I. ARBITRATION AND THE PROBLEM OF SUBSTANTIVE LAW

Arbitration as a means of settling commercial disputes between parties of different nationalities has been a popular and successful alternative to national courts for decades. Parties entering into economic agreements often include arbitration clauses in their contracts to ensure that any disputes can be solved without recourse to expensive and time-consuming litigation. Moreover, arbitration allows Parties to avoid having disputes judged in the national courts of the opposing party. It is not surprising, therefore, that the rise in international commerce and investment in recent years has brought an increased use of arbitration to resolve disputes.

Arbitration in the international context involves numerous difficulties, one of the most troublesome of which is the choice
of substantive law to be applied in a given dispute. The substantive law of the arbitration may be specified by the parties in their original agreement. In general, parties to an agreement containing an arbitration clause have virtually complete autonomy in selecting the substantive governing law; almost any choice of substantive law by the parties is enforceable, so long as the arbitral award itself is enforceable. Absent an express or implied choice by the parties, the governing law may be chosen by the arbitrator. Although parties frequently specify the law of a particular jurisdiction as the background law governing the merits of any dispute, they often supplement such a choice, or avoid it altogether, by referring to lex mercatoria, customs of the trade, or general principles of law. Of these three substantive schemes, the last is especially vague because of its broad scope and lack of explication in the literature. Particularly because there is no delineated set of general principles, results become unpredictable, and parties to agreements have little ground on which to base their expectations. Moreover, because general principles of law are an especially popular choice of substantive law when sovereign governments are involved in an agreement, and because such agreements are likely to proliferate as developing nations make long-term economic development contracts with companies from industrial nations, the application of this term will become an even more important issue.

II. CHOOSING THE SUBSTANTIVE LAW

A. When Parties Specify a National Law

When the parties clearly designate the substantive law of a particular jurisdiction, there is little room for the application of general principles of law. Nor would there be much justification for the imposition of such principles, as the agreement by the parties on an explicit, developed national law exhibits a common understanding of or familiarity with such law, as well as an intention to be bound specifically to a relatively inflexible standard.

It does not follow, however, that a national law is the best choice of substantive law available, for national laws may suffer from a variety of shortcomings in the context of international trade and investment. Some national laws may not be sufficiently developed to provide a basis for international transactions; even sophisticated national systems may be conducive only to domestic transactions. Other national laws may promote the national interest at the expense of private parties. Finally, the political realities in some nations make resort to national law unacceptably risky from the standpoint of a private contracting party, even though the law is acceptable at the time of contracting. For these reasons or because they cannot agree on any particular national law, parties may wish to allow the arbitral tribunal to apply a substantive law not tied to any particular jurisdiction.

Yet in some cases reference to a non-national standard, much less to arbitration, is unavailable because of these very political realities. In the case of Latin America, the Calvo Doctrine traditionally has held that foreigners may receive treatment only equal to that of citizens. Because international arbitration often gives foreigners but not citizens a right to arbitrate disputes, the Calvo Doctrine has opposed arbitration on the ground that it gives preferential treatment to foreign investors. Even more broadly, the historical legacies of the Calvo Doctrine and the Latin Americans' strict defense of national sovereignty have translated into a refusal to accept the application of general principles of international law in the Latin American context.

B. When Parties Allow a Non-National Standard

The parties may supplement their choice of a national law with reference to some non-national standard such as general
principles of law, *lex mercatoria*, or the law of international trade, or they may specify only a non-national standard, without referring to any national law. Either choice grants the arbitral tribunal more discretion with respect to the applicable law, but correlatively provides it with a diminished level of guidance. In either case, the arbitrator is forced to abandon a simple application of specific rules contained in a national law and instead to conduct an initial inquiry to determine the nature of the general principles invoked by the parties. Thus, the arbitrator in such cases must conduct an analysis to discover the principles to be applied under the often vague, non-national Standards.

C. When the Agreement Is Silent as to Substantive Law

In many cases the parties simply are unable to agree on a particular national or non-national law and are willing to put off any conflict over the applicable law until the need arises. Arbitrators in such situations have more discretion than in any other case, as they may apply any substantive law that their arbitral rules and other procedural provisions allow. Traditionally, scholars believed that the arbitrator was bound to apply the conflict-of-laws system where the arbitral tribunal had its seat, but recently this view has been challenged; instead, arbitral tribunals now frequently apply the conflict-of-laws system they view most appropriate.

Alternatively, arbitrators may apply a variety of other conflict-of-laws standards that have only an indirect foundation in national law. The least significant departure from a national conflict-of-laws system is the cumulative application of the conflict-of-laws systems connected with the dispute. A more substantial departure is the application of the conflict-of-laws system the arbitrator views as most appropriate and most responsive to international commerce. A third, still greater departure is the application of a basic conflict-of-laws rule derived from a comparison of competing systems. The last step before attaining a fully denationalized arbitral procedure is the application of a substantive national law without reference to any conflict-of-laws system.

Finally, in the absence of any choice of Substantive law by the parties, an arbitrator in some cases may apply a fully non-national standard such as *lex mercatoria*, standard usages, or general principles of law. In general, two elements in a contract might permit the application of such a non-national standard. First, the existence of an arbitration clause in an international transaction, together with the international character of the dispute and the reasons that parties choose arbitration to resolve disputes, although not sufficient to ensure the exclusive use of a non-national law to govern the agreement, provide a basis for the use, albeit nonexclusive, of non-national law in arbitrating the dispute. Second, when considering disputes over economic development agreements, particularly those containing stabilization clauses that limit a sovereign's capacity to alter the rights of the private party, arbitrators invoke a non-national standard to assess the validity of the stabilization clause in order to protect the private party's rights.

When the arbitrator is free to choose and interpret any such non-national law, the arbitrator's inquiry must begin with the discovery and derivation of the general principles of law. Because there is no clearly delineated set of general principles, it is uncertain at the time of contracting what general principles will govern disputes arising under the agreement. Herein lies the greatest weakness of the use of non-national law: it creates uncertainty in arbitral decisionmaking, with the ultimate result that parties to such agreements are unable to predict confidently the legality of their actions before arbitration. Here, too, lies the strongest argument for developing a coherent set of principles based on published arbitral awards. Delineating the non-national law of international arbitration would capture the advantages of neutrality and fairness that are the fundamental aim of non-national standards, and at the same time reduce the uncertainty that results from the process of deriving the general principles in each arbitration.

III. DERIVING GENERAL PRINCIPLES OF LAW

This Part seeks to enunciate the fundamental axioms of a non-national law of international arbitration, focusing particularly on the concept of general principles of law. These axioms are most likely to
be applied by tribunals in cases in which at least one of the parties is a sovereign state, but general principles of law may be of use in a private context, as well. In either case, the application of this substantive law presents special problems that the other non-national standards do not, most notably the vagueness and uncertainty that inhere in a "general" standard based loosely on practice.42

The ultimate aim of this listing is to initiate a sustained effort to achieve a consensus as to the content of the general principles of law in the international arbitration context. This consensus would lead to greater consistency of results in international commercial arbitrations and to a corresponding increase in certainty for contracting parties.43 Ultimately, it also may encourage greater reference to the general principles of law. This would serve the interests of contracting parties by enabling them to establish a neutral forum in which they control the language and procedure and avoid the various difficulties that arise from handling such disputes in a national court system. At the same time, a list of general principles will help maintain the stability and certainty that exist in a system currently dominated by national laws.

A. Jurisprudence and Methodology

The traditional approach in the secondary literature to the problem of general principles of law has been to discuss the choice-of-law issue and to suggest possible justifications for applying such a general substantive standard.44 However, if these justifications are legitimate, a more important task involves defining the general principles that make up such a standard. In the arbitration context, the best indication of the acceptance of a proposition as a general principle is its frequent invocation by arbitral tribunals and its recognition by scholars. Using such sources, along with occasional references to national practice to

predict outcomes when arbitral decisions have not yet confirmed the universality of such principles, this Note attempts to delineate some of the most basic tenets. To date, despite references to general principles, the literature does not contain any listing of these principles.45

Because parties often expressly require confidentiality, any attempt to delineate a list of general principles of law in the context of international commercial arbitration will be limited by the paucity of published arbitral awards. There is, however, a sufficient number of publicly available cases to begin the endeavor; in time, the list may be expanded as more information about arbitral awards becomes available. This Note catalogues approximately twenty awards of widely varying types that have been reprinted in the secondary literature or incorporated into the index sections of major arbitration reporters.46 These cases include some involving only private parties and others involving sovereign governments. They also include institutional arbitrations conducted under the aegis of the American Arbitration Association, the ICC, or ICSID, as well as ad hoc arbitrations conducted under the rules of UNCITRAL, the American Arbitration Association, or the ICC.47 Thus, although the sample is numerically limited, it is nonetheless broad.

Because foreign private parties frequently prefer general principles of law as the binding substantive law when entering into agreements with sovereign governments, and because arbitrations between such parties frequently involve nationalizations, this Note relies in part on arbitral awards based on disputes arising from nationalizations. Discussion of these disputes sheds light on a number of general principles. In the transactions that ultimately give rise to arbitrations, transfers of property rights from a sovereign to a foreign private party have almost always been through an express contractual agreement. In these situations, nationalization can be regarded as both a breach of contract and as a taking of property. In such cases, the issue first arises whether the particular investment or trade arrangement granting property rights constitutes a binding contract. If so, two additional questions are raised: first, whether the governmental action in question constitutes a breach of the contract; and second, whether the

breach constitutes a taking of property compensable under international law. Thus, the nationalization cases can animate a general discussion of such principles.

B. Some General Principles of Law

One difficulty that arises in delineating a set of general principles of law is that many of these principles are interrelated. In an effort to overcome this problem, this Note presents the principles separately but discusses their relationship to each other. What follows are seven general principles: five govern international contractual agreements, the means of assigning liability, limits on the enforceability of contracts, and remedies in case of breach; one describes the limits on the right of a
sorveign to take the property or to encroach upon the vested rights of a foreign private party; and one describes the 
theory of unjust enrichment that pertains in the absence of a contractual agreement or grant of property.

1. **A sovereign government may make and be bound by contractual agreements with foreign Private Parties.** - 
Governments may enter into contractual agreements with foreign private parties without negating their sovereignty; 
indeed, such commitments are viewed as reaffirmations of states' sovereign power of self-determination.48 Thus, 
claims of sovereignty are not ordinarily allowed as means to disregard earlier contractual commitments, at least in 
the commercial context.49

2. **The corporate veil may be pierced to prevent a beneficial owner from escaping contractual liability.** - Equity and the 
principles of international law permit the corporate veil to be lifted to protect third parties such as creditors or 
purchasers against abuses that would harm them directly, at least in the case of a corporation that is emptied of its 
assets by the parent.58 In the Westland decision, the United Arab Emirates, Saudi Arabia, and Qatar, in response to 
the Camp David Agreement, had liquidated the - Arab Organization for Industrialization, a multilateral organization 
of several Arab states including Egypt that engaged in joint ventures for the development of an arms industry.59 The 
tribunal held that Westland was justified in bringing the former members of the organization to arbitration 
notwithstanding the fact that only the organization itself had signed the agreement.60

3. **Force majeure**61 justifies nonperformance of a contract such that the loss is borne fairly by the parties. - The 
ocurrence of a force majeure renders nonperformance not a breach. However, the loss from the force majeure 
must be borne fairly by the parties.62 There is nonetheless little international agreement as to what constitutes force 
majeure, so this principle as yet offers little specific guidance.

4. **Referring Principles:**
   - IV.2.3 - No repudiation of contractual consent by state party
   - IV.7.1 - Invalidity of contract that violates good morals ("<em>boni mores"</em>)
   - VI.3 - Force majeure
   - IX.1 - Basic rule
   - X.2 - Piercing the corporate veil
   - XI.1 - Compensation for expropriation