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THE PREDICTABILITY PARADOX: ARBITRATORS AND APPLICABLE LAW

Forthcoming in *11 ICC Dossiers (ICC Institute of World Business Law 2014),
Proceedings of Annual Meeting on International Arbitration and Substantive Applicable Law*
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The Predictability Paradox:
Arbitrators and Applicable Law

William W. Park*

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I. When Contract Terms Collide

A. Starting Points for Authority

More than a half century ago, a Hungarian psychoanalyst suggested terms to distinguish between thrill seekers and those who cling to the predictable: the ‘philobat’ who enjoys departing from the safe and predictable, and the ‘ocnophile’ who clings to stability.¹ The latter category includes the risk averse (or just plain prudent) individuals who accept the prospect of being up

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¹ Michael Balint, *Thrills and Regressions* (1959). Balint coined the first term as a variant of acrobat, one who walks away from the safe earth, and the second from the Greek root *ocno* in the verb “to cling” or “to hesitate”. *Id.* at 25. Popularized explorations of the thesis appeared in Daniel Goleman, ‘Saying Goodbye Speaks Volumes’, *New York Times* (3 April 1984); Daniel Goleman, ‘Leaving’, *International Herald Tribune*, 7-8 April 1984, at 18.

only one dollar (rather than two) in order to attenuate the possibility of having nothing at all.²

Much of the impulse to arbitrate international disputes might be explained as a response to specters of uncertainty, whether lying in the ‘hometown justice’ of another country’s judicial system, or the perceived volatility of a civil jury in a faraway land. In the face of such hesitations, arbitration has been pressed into service to create more level litigation playing fields and to reduce the risk of random results.³ The inclination toward certainty and reliability might also explain differences in how arbitrators and judges approach application of national law.⁴ Although perceptions exist in some quarters that arbitrators may be less reliable than judges in applying the law, the opposite may be true.

This gap between reality and perception arises in part because of oft-repeated contentions

² To illustrate the point, a group of students might be asked whether they would work as research assistant for the professor. If the majority raises their hands to signify interest, a quite different response would be expected to a counter-proposal that payment be deferred to the end of the academic year when a coin toss would determine whether they received, in the alternative, double compensation or no payment at all.

³ Those engaged in international transactions tend to think in relative terms, with a rule deemed reliable if it reduces the likelihood of alternate outcomes, not because it operates with perfect foreseeability. Any legal system may, on some issues, work to one side’s disadvantage in a particular case. However, an agreement to ‘play by the rules’ of a relatively evolved system of law in a neutral forum will normally maximize both parties’ *ex ante* expectation of fair treatment. See William W. Park, ‘Neutrality, Predictability and Economic Cooperation’, *Journal of International Arbitration*, 12 (No. 4), 1995, page 99; *Arbitration of International Business Disputes* (2d Ed. 2012), chapter III-B-2, Ch.II-A-2; ‘Arbitration’s Protean Nature: The Value of Rules and the Risks of Discretion (The 2002 Freshfields Lecture)’, *Arbitration International*, 19, 2003, page 279.

⁴ For a general overview of how arbitrators’ interpretation of contract overlaps with their construction of applicable law, see Laurent Lévy & Fabrice Robert-Tissot, *L’interprétation arbitrale*, 2013 (no. 4) Rev. de l’arbitrage 861. The authors compare commercial, sport and investor-state arbitration. Their conclusions suggest, *inter alia*, that for international commercial transactions, arbitrators tend to put more emphasis on the terms of the contract itself than on applicable law.

that arbitrators ‘split the baby’ through awards not justified in law.⁵ Certain strains of literature assert, without any real substantiation, that arbitrators render unprincipled decisions in order to attract business through reappointment.⁶ In fact, no empirical data permits a conclusion on the matter, at least not from variations in records of ‘win rates’ to the extent they can be determined or the size of damages in arbitration as opposed to court litigation.⁷

Just as significantly, the greater reliability often found in arbitral awards, as contrasted with court judgments, derives from different notions of ‘law’ in commercial transactions. The calculus of duty is simply not the same as between judge and arbitrator. Bearing obligations to the citizenry as a whole, judges may seek to implement societal values that sometimes trump private agreements. Although responsible judges will master existing authority before taking the law in new directions, many traditions allow appellate judges to overrule precedent. In some legal systems, judicial policy predispositions have led political scientists to engage in intricate

⁵ The imagery of baby-splitting seems to originate in the Biblical child custody dispute decided in ancient Jerusalem by King Solomon. When one woman accused another of stealing her baby, the King called for a sword so the child might be divided in two, with one half for each woman. Of course, the metaphor hides the character of Solomon’s decision as an interim award, followed by grant of custody to the real mother whose compassion led to abandonment of her claim in hopes of saving her son. 1 Kings 3:23–28.

⁶ See e.g., Richard A. Posner, *How Judges Think* (2008), at 127–128, stating that courts and juries are “more likely to adhere to the law and less likely than arbitrators to ‘split the difference’ between the two sides thereby lowering damages.” As authority for this sweeping assertion, Judge Posner simply quotes a California state case, *Armendariz v. Foundation Health Psychare Services*, 6 P.3d 669, 693 (Cal. 2000).

⁷ See e.g., Daphna Kapeliuk, ‘The Repeat Appointment Factor,’ 96 *Cornell Law Review*, 47 (2010), analyzing 131 ICSID cases implicating almost 200 arbitrators, refuting the oft-banded suggestion that arbitrators either act in a biased way (to please appointers) or render decisions giving each party a partial victory to increase user satisfaction. The author suggests that an arbitrator’s incentive to maintain a reputation for independence and credibility trumps any temptation to act in an inappropriate way. See also Theodore Eisenberg & Elizabeth Hill, *Arbitration & Litigation of Employment Claims: An Empirical Comparison*, 58 DISP. RES. J. 44 (ABA, Nov 2003-Jan 2004), looking at state and federal court trials as compared with AAA arbitrations.

charting of ideology in court judgments.⁸

No similar social engineering usually falls to arbitrators. As creatures of the parties' consent, arbitrators must show special fidelity to shared expectations expressed in contract or treaty, fixing their eyes on existing norms rather than proposals for the law as it should be.

This 'predictability paradox' often demonstrates itself when relatively clear and specific contract language competes with more general provisions of national law. In such instances, arbitrators in international cases may show a heightened sensitivity toward the predictability of contract terms. Although sensitive to public values, rejecting complicity with illicit schemes and abusive procedures, arbitrators fix their eyes more on existing legal norms, asking what the parties had a right to expect. When interpreting the law, arbitrators may be more inclined to take statutes and cases as they are, rather than considering public policies that justify shaping or stretching norms to meet new social or economic challenges.

On occasion, the nature of the judicial office may include a perceived institutional duty to embrace public interests of the forum, or a political inclination to develop the law in light of evolving national concerns of a social or economic nature.⁹ In a dispute over the price of oil, a

⁸ See e.g., Jeffrey A. Segal & Harold J. Spaeth, *The Supreme Court and the Attitudinal Model Revisited* (Cambridge Univ. Press, 2002). The so-called 'Martin-Quinn Scores' use a scale with negative numbers translating to liberalism and positive numbers translating to conservatism. Thus Justice Douglas, considered a very liberal judge, received an average ideological score of minus 4, while a score of positive 4.30 was accorded the conservative Justice Rehnquist. See generally, Andrew Martin, Kevin Quinn, Lee Epstein, 'The Median Justice on the U.S. Supreme Court', *North Carolina Law Review*, 83, 2005, page 1275; Lee Epstein, Andrew Martin, Kevin Quinn & Jeffrey Segal, 'Ideological Drift among Supreme Court Justices: Who, When and How Important', *Northwestern University Law Review*, 101, 2007, page 1483; Lee Epstein, Tonja Jacobi, 'Super Medians', *Stanford Law Review*, 61, 2008, page 37, 99.

⁹ Contemplating competing loyalties of both judges and arbitrators, one recalls without comment the lines in the Sermon on the Mount: "No one can serve two masters. Either he will hate the one and love the other, or he will be devoted to the one and despise the other." Matthew 6:24

judge in a fuel-importing jurisdiction like Massachusetts could be expected to consider payments by local residents during the bitter cold New England winters.¹⁰ By contrast, arguments for lower fuel costs might be received with greater skepticism by judges from oil producing countries like Venezuela.

Of course, personal sympathies can play a role for both arbitrators and judges.¹¹ For the disciplined arbitrator, however, whether from Boston or from Caracas, the duty toward the contracting parties and the correct interpretation of their agreement will tend to manifest itself in a heightened fidelity to the parties' shared *ex ante* expectations, and thus predictable vindication of contract rights.¹²

Such variations in the approaches of arbitrator and judge tend to be linked to their respective sources of authority. The genesis of judicial power normally lies in the political collectivity that appoints the judge and pays his or her salary.

¹⁰ On occasion, it has been argued that public interests come into play more for investor-state arbitration than for commercial disputes. On reflection, however, contract disputes affect the world's aggregate social and economic welfare no less than investment treaty controversies. If the financial crisis of 2008 demonstrates anything, it teaches that private choices have public consequences. To some extent, the debate may be about terminology. See e.g. 'Theory and Reality of the Arbitrator', *World Arbitration & Mediation Review*, 7, 2013, pages 629-649, including proceedings of the 25th Annual Institution for Transnational Arbitration in Dallas in June 2013. In response to suggestions that both commercial and investor-state arbitration affect public interest, Professor Brigitte Stern replied that commercial cases have "an impact on public interest" whereas "investment arbitration is completely different because the public interest is part of an element of the award." *Id.* at 642.

¹¹ See e.g., Edna Sussman, 'Arbitrator Decision-Making: Unconscious Psychological Influences and What You can Do About Them', *American Review of International Arbitration*, 24, 2013, at page 487.

¹² For a broader treatment of what has been called arbitration's 'ambivalence toward law' see Jan Paulsson, *The Idea of Arbitration* (2013) at 13-18.

By contrast, the arbitrator's legitimacy starts with an agreement to waive recourse to otherwise competent national courts.¹³ At least as to the merits of a dispute, arbitration clauses will normally be construed as a renunciation of judicial decision-making. Such waivers are usually created either by private contracts or through government-to-government treaties.¹⁴

To some extent, this paradox rests on contrasting notions of predictability, opposing contract provisions against notions of the 'right' as perceived in the forum community. The arbitrator may look to enhance shared *ex ante* expectations of the parties themselves, applying the law on an 'as is' basis. By contrast, appellate judge might explore principles that push law into new directions, so as to promote certainty from the perspective of emerging policy.¹⁵

In an international context, bias and fairness often appear as opposite sides of the same coin. The party for which a rule creates commercial disadvantage will welcome a softening of that rule's rigor by a judge in its home forum. By contrast, the foreign side might perceive failure to enforce the bargain as simply xenophobic prejudice.

¹³ As suggested by Professor Pierre Mayer, constraints on the international arbitrator derive from "the will of the parties, the jurisdictional nature of the arbitral function, and in modern legal systems only minimally from mandates at the arbitral seat." Pierre Mayer, 'La liberté de l'arbitre', *Revue de l'arbitrage*, 2, 2013, page 340. In the original, "[*Les contraintes sur l'arbitre*] tiennent à la volonté des parties, à la nature juridictionnelle de sa fonction et, dans les législations modernes, seulement dans une faible mesure à certains impératifs émanant de l'Etat du siège."

¹⁴ This does not mean, of course that courts fail to play a role in monitoring the arbitration process, particularly in connection with the contours of arbitral authority. See e.g., George Bermann, 'The 'Gateway Problem' in International Commercial Arbitration', *Yale Journal of International Law*, 37, 2012, at 1; William W. Park, *Jurisdiction to Determine Jurisdiction*, 13 ICCA Congress Series 55 (Permanent Court of Arbitration, The Hague, 2007). Some legal systems maintain a right of appeal on the legal merits, as for example Section 69 of the 1996 English Arbitration Act.

¹⁵ For example, applicable law might say that fraud in sales contract gives a buyer the right to rescind, but not to seek damages that could in essence be characterized as a price renegotiation. A judge might consider the rule outmoded, and give buyers new rights, whereas the arbitrator might be expected to stick to the law 'as is' rather than as it should be.

Imagine, for example, that a gas supply agreement between an Algerian state agency and a Boston importer operates to the disadvantage of the American buyer. A court judgment refusing to enforce certain aspects of the contractual arrangements might appear as promoting community interests in Massachusetts. From the perspective of the Algerian seller, however, the judicial decision would likely seem to be simply a way to ignore the parties' freely accepted agreement to enhance post-dispute local interests.¹⁶

B. Exculpatory Clauses and Arbitral Jurisdiction: An Illustrative Scenario

As between judge and arbitrator, different results arise most pointedly when express terms of an agreement appear to conflict with mandates of the contractually chosen law. For example, an international sales contract contains explicit language providing that neither side shall be liable in damages for negligence, including gross negligence. The contract's clear exculpatory language has been reinforced by an unequivocal arbitration clause stating that the arbitrator has no authority to award damages for negligence of any kind. However, the contract also provides for its interpretation according to the law of a third-country legal system not that of either party, which invalidates any purported contractual exclusion of responsibility for gross negligence.

What should happen if one side claims damages for gross negligence? A judge in Geneva or Boston would normally interpret such exculpatory language under the law of Switzerland or Massachusetts, each of which invalidates such exculpatory clauses.¹⁷ Absent a choice-of-law rule

¹⁶ See e.g., *Sonatrach v. Distrigas*, 80 Bankr. 606 (D. Mass. 1987). In reversing a lower court decision which, at the request of the Massachusetts importer, had denied enforcement of an arbitration agreement invoked by the Algerian seller, the Federal District Court for Massachusetts opined, "It is important and necessary for the United States to hold its domiciliaries to their bargains and not allow them to escape their commercial obligations by ducking into statutory safe harbors." *Id.* at 614.

¹⁷ Swiss *Code des Obligations* (Book V, Code Civil), Art. 100(1): "*Est nulle toute stipulation tendant à libérer d'avance le débiteur de la responsabilité qu'il encourrait en cas de dol ou de*

directing a different result, courts would be hard pressed not to disregard the damages limits given that the state creating their authority outlawed the restrictions.

By contrast, an arbitrator might accord more deference the contract terms as indicative of party-imposed limitations on arbitral jurisdiction. Specific stipulations usually trump more general principles.¹⁸ The exclusion of jurisdiction with respect to negligence damages would at first blush seem narrower and more specific than a general reference to an applicable law. Thus the arbitrator might decide that the litigants intended the chosen law (Massachusetts or Switzerland) to fill gaps, but not to contradict explicit contract restrictions on arbitral authority. The arbitrator's authority to apply an applicable law comes into play by virtue of the parties'

faute grave." (Any agreement purporting to exclude in advance liability for willful blindness or gross negligence is void.) See also *Zavras v. Capeway Rovers Motorcycle Club*, 687 N.E.2d 1263, 1265 (Mass. App. Ct. 1997). A rider was injured while competing in a motorcycle race, crashing at a jump without knowing that a previous accident had created a pile-up in the landing zone. The motorcycle club allegedly employed a flagman who failed properly to warn of the pile-up. Although the rider agreed in writing to hold the club blameless for any loss or injury, the court found gross negligence cannot be waived.

¹⁸ For a broader musing on the benefits of specific as contrasted with general rules, see Antonin Scalia, *The Rule of Law as the Law of Rules*, 56 U. CHICAGO LAW REV. 1175 (1989), contrasting rules of law with personal discretion to do justice, the latter having been exemplified in the fair and even-handed decisions dispensed by King Louis IX of France sitting under his proverbial oak tree in the summer after having heard mass.

agreement, rather than the mandates of a forum imposing itself *sua sponte*.¹⁹ Moreover, an award that disregards the exclusion of liability could result in annulment for excess of jurisdiction.²⁰

Of course, good arbitrators avoid any simplistic vision of the parties' intent that gives *a priori* precedence to either substantive contract terms or a choice of otherwise applicable legal principles. In some instances, seeming inconsistencies may, on deeper reflection, reveal themselves as false conflicts.²¹ The devil remains very much in the details of each case.

For international cases, the lodestar of party intent can prove particularly elusive. A contract between Finns and Turks might be drafted in English, not the mother tongue of either side's business managers. The agreement might then be subject to the law of Switzerland simply for 'neutrality' reasons, although the transaction had no connection with the Helvetic Confederation. The choice of law clause may have been inserted about 2:18am, at the end of long negotiations when the main business points of price and delivery had been agreed, leaving

¹⁹ Such an illustration assumes of course that the contract terms do not run afoul of mandatory norms at the place of performance, often called '*lois de police*' by Continental scholars. See Pierre Mayer, 'L'arbitre international et la hiérarchie des norms', *Revue de l'arbitrage*, 2, 2011, page 361. In *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 637 n.19 (U.S. 1985), the Supreme Court stated "in the event the choice-of-forum and choice-of-law clauses operated in tandem as a prospective waiver of a party's right to pursue statutory remedies for antitrust violations, [it] would have little hesitation in condemning the agreement as against public policy."

²⁰ One can only speculate about the fate of separate negligence claims brought in court following an arbitrator's decision that such damages lie outside arbitral competence.

²¹ In many instances, of course, waivers remain compatible with applicable law. For example, the law of New York provides that a contracting party may explicitly disclaim reliance on any statements or nondisclosures, albeit with an exception related to "facts allegedly misrepresented [that lie] peculiarly within the seller's knowledge." See *Manu. Hanover Trust v. Yanakas*, 7 F.3d 310 (2d. Cir. 1993); *DIMON Inc. v. Folium, Inc.*, 48 F. Supp. 2d 359, 368 (S.D.N.Y. 1999); *MBIA Ins. Corp. v. Royal Bank of Can.*, 28 Misc. 3d 1225(A), 1225A (N.Y. Sup. Ct. 2010). An arbitrator considering a fraud defense with respect to a contract governed by New York law would normally take into account not only the waivers, but also arguments about the 'peculiar knowledge' of the seller.

drafting teams with little time to study what the Swiss law might say about a potentially controverted matter.²²

Finally, the matter of arbitration language injects another significant difference between the arbitrator and the national judge in an international context. In addition to the words used in presenting argument and evidence, language can also affect the procedural framework of a case. For example, testimony might be heard in French, but in an arbitration built on the procedural language of American practice dominated by document production unknown in the French legal system. Moreover, words such as ‘witness’ and ‘*témoïn*’ may prove false friends if evidence is presented by a party’s employee, lacking capacity to testify under French legal concepts.²³

C. Tools for Interpretation

In many instances of course judicial and arbitral interpretation will run along similar lines, most notably when law serves to assist contract construction by providing hermeneutic tools. Divergence between judge and arbitrator will be less likely when the law serves merely to provide interpretative or exegetical principles.

²² The construction exercise becomes more complex if the parties choose to import only part of a third country law. For example, English and Belgian companies might stipulate to contract interpretation under Book V of the Swiss Civil Code, the ‘Code of Obligations’ governing commercial matters. Difficult questions arise if arbitrators applying that choice of laws clause receive an application to adapt contract terms pursuant to Book I of the Civil Code, containing the well-known Article 2 on good faith and abuse of rights. Depending on context, an argument can be made that explicit choice of Book V alone serves to exclude other parts of Swiss law.

²³ See Yves Derains, ‘Langue et langages de l’arbitrage’, *Mélanges en l’Honneur de Pierre Tercier* 789 (P. Guach, F. Werro, & P. Pichonnaz, eds., 2008). Compare Pierre A Karrer, ‘Arbitration and Language: Look for Purpose’, 11 *Croatian Arbitration Yearbook* 7 (Zagreb 2004), addressing matters such as the language use for taking evidence and the risks of mistranslation. See also Nicolas C. Ulmer, ‘Language Truth and Arbitral Accuracy’, *Journal of International Arbitration*, 28, 2011, at page 285. For a somewhat broader take on the interaction of language and interpretation of legal texts, see Larry Alexander & Saikrishna Prakash, ‘Is That English You’re Speaking? Why Intention Free Interpretation is an Impossibility’, *San Diego Law Review*, 41, 2004, at page 967.

Imagine for example that a manufacturer seeks to end a distributorship on the basis that products were late getting to customers. The distributor contends that since contract inception, a two-week delivery practice been deemed reasonable, with recent insistence on shorter periods serving as mere pretext for unauthorized termination.

At least in some contexts, New York law provides that post-contract behavior may serve to inform understanding in the meaning of contract terms. For example, when a sales contract involves repeated occasions for performance, with knowledge of the nature of the performance and the opportunity for objections, any such course of performance “accepted or acquiesced in without objection shall be relevant to determine the meaning of the agreement.”²⁴

Regardless of where they might be sitting, conscientious arbitrators, construing a contract pursuant to New York law, would normally take account of a course of performance, just as would New York judges. The chosen law serves as an instrument for exegesis of the contract terms, not as a source of independent duties.

II. Knowing the Law

A. Precedent and Policy

Application of the law by arbitrators and judges often occurs in the shadow of divergent ways that law may be known,²⁵ proved,²⁶ or in some instances presumed.²⁷ In theory no law will

²⁴ See UCC Section 2-208(1) as enacted in New York.

²⁵ See Gabrielle Kaufmann-Kohler, ‘Iura Novit Arbitrator: Est-ce bien raisonnable? Réflexions sur le statut du droit de fond devant l’arbitre international’, in *De Lege Ferenda: Etudes pour le professeur Alain Hirsch* 71 (A. Héritier Lachat & L. Hirsch, eds., 2004); Gabrielle Kaufmann-Kohler, ‘The Arbitrator and the Law’, *Arbitration International*, 21, 2005, page 631; Julian D. M. Lew, ‘Proof of Applicable Law in International Commercial Arbitration’, in *Festschrift für Otto Sandrock* 581 (K. P. Berger, W. F. Ebke, S. Elsing, B. Grossfeld, & G. Kühne, eds., 2000).

²⁶ Although judges are often presumed to know the law under the principle of *jura novit curia*, the position in England, where foreign law will normally be proved as fact (Rule 18, Dicey,

be ‘foreign’ to an international tribunal. In practice, however, the applicable law may be unfamiliar to some members of the tribunal, who may need to be instructed by experts.²⁸

Normally, the process for such instruction might take the form of testimony from learned professors or practitioners, presented by each side. In some instances, the arbitrators will engage in direct study of legal authorities and theories. This does not mean that an arbitrator’s conclusions should contain surprises from such self-instruction. Providing an opportunity for the litigants to comment on the law remains vital both to the arbitrator getting it right and to the parties’ sense of being treated justly.²⁹

Morris & Collins, *The Conflict of Laws* (Lawrence Collins, Gen. Ed., 14th ed. 2006), Chapter 9 pages 255 et seq.) while in the United States Rule 44.1 of the U.S. Federal Rules of Civil Procedure provides that courts in determining foreign law “may consider any relevant material or source, including testimony, whether or not submitted by a party or admissible under the Federal Rules of Evidence.” Similar state law principles include New York CPLR § 4511 and Massachusetts GL Ch. 233, § 70, directing courts to take judicial notice of foreign law.

²⁷ Instances where eminent judges and arbitrators simply presume a conclusion are not hard to find. See *Petroleum Development (Trucial Coast) Ltd. and the Sheikh of Abu Dhabi*, *International & Comparative Law Quarterly*, 1, 1952, page 247, where Lord Asquith of Bishopstone admitted that the applicable system of law was *prima facie* that of Abu Dhabi, then added, “But no such law can reasonably be said to exist. The Sheikh administers a purely discretionary justice with assistance of the Koran; and it would be fanciful to suggest that in this very primitive region there is any settled body of legal principles applicable to the construction of modern commercial instruments.” See generally, Ibrahim Fadlallah, ‘Arbitration Facing Conflicts of Culture’, *Arbitration International*, 25, 2009, page 303.

²⁸ In a dispute between a Chinese state entity and an investor from the United States, with the contract subject to the law of China, the American party might appoint as arbitrator a New York trained lawyer who would sit with a Chinese jurist appointed by the state entity, and a third-country national as chair.

²⁹ The rule that parties must have a chance to comment on applicable law was explored *inter alia* by the highest court in France in *Commercial Caribbean Niquel v. La Société Overseas Mining Investments*, Arrêt No. 785, 29 June 2011, Court de Cassation, Première chambre civile, rejecting challenge to the decision of the Cour d’appel de Paris, ch. 1, 25 March 2010, discussed in Seranglini, *La Semaine Juridique Ed. G.*, No. 23, 7 juin 2010. The case addresses an award based on a damages theory of ‘lost change’ rather than ‘lost profits’ in mining ventures. See generally, William W. Park, *Arbitration of International Business Disputes* (2d Ed. 2012), chapter 1 (at 8-10).

Notions of precedent play themselves out differently in arbitration as contrasted with court litigation. Within a single national jurisdiction, a measure of uniformity can be imposed on courts from the top down. One case furnishes authority for decisions in similar fact patterns with similar questions of law. Although in theory Continental and ‘common law’ traditions take divergent views of precedent, with the former giving lower courts considerable autonomy to interpret legal texts *de novo*,³⁰ in practice Continental judges remain mindful of higher court decisions.³¹

By contrast, absent *res judicata* or issue preclusion arising for the same parties and the same claims or issues,³² arbitrators do not usually deem themselves bound by rulings of other tribunals in the way judges feel constrained by decisions of superior courts in a unified and hierarchical national system.

This does not mean that prior awards will be ignored. To the contrary, decisions of other arbitral tribunals are often taken into account as constituting a corpus of principles representing the litigants’ shared expectations. While not given the status of precedent in a narrow common

³⁰ Article 5 of French *Code civil* forbids judges from purporting to make general rules: *Il est défendu aux juges de prononcer par voie de disposition générale et réglementaire sur les causes qui leur sont soumises*. A similar principle applies in Germany. See Klaus-Peter Berger, ‘To What Extent Should Arbitrators Respect Domestic Law? The German Experience Regarding the Law on Standard Terms’, forthcoming in *Arbitration International*, 30, 2014, looking *inter alia* at application of German case law relating to limitation of liability (‘cap’) clause in standard form agreements.

³¹ See generally, Denis Tallon, ‘Précedent’, in *Dictionnaire de la Culture Juridique* 1185-1187 (2003).

³² While *res judicata* prevents the same parties from re-litigating the same cause of action after it has already been adjudicated in an earlier lawsuit, notions of issue preclusion come into play when a second but different lawsuit implicates questions decided in a prior action, the re-litigation of which questions is then barred. French doctrines of *force de chose jugée* and German concepts of *rechtskräftiges Urteil* play roles similar to those of *res judicata* in the common law tradition.

law sense, awards of respected arbitrators may bolster support for results in other cases,³³ providing information about what the relevant community considers the right approach to similar problems.³⁴ For litigants, this information can serve as a tool of persuasion. For business managers and government planners, it provides one way to predict how future disputes will be resolved. And for the arbitrators, prior rulings can justify awards to the rest of the world and enhance the prospect that similar cases will be treated similarly.³⁵

Finally, the relationship between questions of law and fact remains slippery in any context,³⁶ and may prove a challenge to judges and arbitrators alike. Controverted facts can

³³ One authority has suggested that for international arbitration precedent exists as “decisional authority that may reasonably serve to justify the arbitrators’ decision to the principal audience for that decision.” Barton Legum, ‘Definitions of Precedent in International Arbitration’, in *Precedent in International Arbitration* (E. Gaillard & Y. Banifatemi, eds. 2008) 5, 14.

³⁴ For an illustration of the delicate ambivalence arbitrators feel about prior awards, see *AES Corporation v. the Argentine Republic*, ICSID Case No. ARB/02/17, Decision on Jurisdiction, ¶ 30 (Jul. 13, 2005), which asserts that each arbitral tribunal “remains sovereign and may retain, as it is confirmed by ICSID practice, a different solution for resolving the same problem...” Following a semicolon, the sentence then adds that decisions “dealing with the same or very similar issues may at least indicate some lines of reasoning of real interest; this Tribunal may consider them in order to compare its own position with those already adopted by its predecessors and, if it shares the views already expressed by one or more of these tribunals on a specific point of law, it is free to adopt the same solution.” *Id.*, page 11.

³⁵ For investor-state treaty disputes, jurisdictional questions such as ‘most-favored nation’ prove fertile sources for *de facto* precedent. See Tai-Heng Cheng, ‘Precedent and Control in Investment Treaty Arbitration’, *Fordham International Law Journal*, 30, 2007; Jeffrey P. Commission, ‘Precedent in Investment Treaty Arbitration’, *Journal of International Arbitration*, 24(2), 2007, page 129. Precedent is also common in ‘trade arbitration’ (maritime, commodities and reinsurance). See Michael Marks Cohen, Letter, 10 (No. 2) INT’L ARB Q. L. REV 113 (Summer 2009).

³⁶ In *Vargas v. Insurance Co. of North America*, 651 F.2d 838 (2d Cir. 1981), an aviation policy covered accidents “within the United States of America.” The insured died while traveling between two points of the United States (New York and Puerto Rico), invoking a canon of construction requiring ambiguities to be resolved against the drafters (*contra proferentem*) that has since been excluded in many liability policies. See also Gerald Leonard, ‘Rape, Murder, and Formalism: What Happens When We Define Mistake of Law?’ *University of Colorado Law Review*, 72, 2001, page 507, commenting on the English rape case *Regina v. Morgan* where a

remain stubbornly particular, requiring recourse to witnesses and exhibits, while the law by its nature possesses a generality that permits instruction by reading statutes and cases.³⁷

B. Procedural Norms

In some instances, arbitrators must interpret and apply national law provisions imposing constraints on procedural matters, rather than substantive norms of contract construction. In that context, the duty of fidelity to the parties' agreement may compete with the obligation to comply with mandatory procedures of the arbitral seat. Or the arbitrators may interpret national arbitration law in a way at odds with the view of the local judiciary.³⁸

The first dilemma (potential conflict between contract and procedural law) exemplifies itself in provisions English arbitration law invalidates pre-dispute agreements to allocate

defendant's incorrect belief that a woman consented would be a defense, but not an incorrect understanding of the law.

³⁷ In a sense, we cannot say what the law is for a given dispute until first knowing what law is in general. One working definition articulates law as an authoritative dispute resolution process that includes principles for substantive conduct as well as procedures for deciding cases.

Francophone jurists distinguish between '*loi*' and '*droit*' both of which are 'law' for the Anglophone. A tyrant's statute ('*loi*') might be law in the sense of an enactment, while contrary to authoritative norms ('*droit*') recognized from a more legitimate vantage point. English King George III may have made such a distinction for laws of his rebellious American colonies, as did the colonists for some British taxes before 1776.

³⁸ In some instances the relevant legal provision might lie on the border of procedure and substance, to be called into question only in the event of perceived ambiguity in contract terms. See e.g., the exclusionary rule interpreted by the British House of Lords (as it then was) barring evidence of the parties' subjective intentions that predates an agreement. See *Investors Compensation Scheme v. West Bromwich Building Society*, [1998] 1 All ER 98, [1998] 1 WLR 896, [1997] UKHL 28, [1998] WLR 896; *Charbrook v. Persimmon Homes* [2009] UKHL 38, paragraphs 41-42 as per Lord Hoffmann. Compare Article 1341 of the French *Code civil* which prohibits witness testimony to modify clear terms of a contract in the event of property conveyances made by notarial deed. For related French provisions on contract interpretation, see *Code civil* Articles 1156 (*la commune intention des parties*) and 1157 (*effet utile*).

arbitration costs ‘in any event.’³⁹ In advance of the dispute, parties may not by contract forbid an arbitrator from allocating costs on the basis of who won and who lost. The provision casts a wide net, catching even reasonable arrangements among sophisticated business managers to split arbitrator compensation on a 50/50 basis and to require each side to cover its own legal expenses.

In such an instance, where the contract terms fix cost principles, what is to be done by a conscientious arbitrator? Aiming to respect the parties’ agreement, an arbitrator would let the costs lie where they fall. Yet to do so might run the risk of award annulment if proceedings are seated in London.

To complicate matters, disregard of the parties’ *ex ante* expectations may appear as excess of authority to a New York court called to enforce an award of legal costs inconsistent with the terms of the agreement and the applicable law, putting the arbitrators between Scylla and Charybdis when the award must be enforced in a jurisdiction that values respect for the parties’ choices.⁴⁰

The second problem (possible tension between arbitral and judicial interpretations of procedural mandates) finds illustration in the vexing subject of “class arbitration” and supplies another dimension in the slippery task of interpreting national procedural law. The United States

³⁹ Section 60, Arbitration Act of 1996: “An agreement which has the effect that a party is to pay the whole or part of the costs of the arbitration in any event is only valid if made after the dispute in question has arisen.” Section 61 goes on to set forth the general principle that “costs should follow the event except where it appears to the tribunal that in the circumstances this is not appropriate in relation to the whole or part of the costs.” This standard, however, is made subject to the parties’ agreement otherwise, which in context with Section 60 would be an agreement after the dispute has arisen. The rule’s most understandable application would be as an anti-abuse mechanism to prevent clauses that would require weaker parties to pay all costs, thus discouraging otherwise legitimate claims.

⁴⁰ The scenario of London arbitral *situs* with New York substantive law occurs frequently in contracts between American policyholders and British insurers, the so-called ‘Bermuda Form’ arbitrations discussed in Richard Jacobs, Lorelie S. Masters & Paul Stanley, *Liability Insurance in International Arbitration* (2004; 2d Ed. 2011).

Supreme Court addressed the matter in an action arising from price-fixing allegations against ship owners brought by customers who chartered vessels commonly known as ‘Parcel Tankers’ to transport food oils and chemicals.⁴¹

In connection with the customers’ request for a single arbitration proceeding (‘class arbitration’ borrowing language from American court procedures⁴²), the arbitrators in a partial award interpreted both the contract and the Federal Arbitration Act to permit class arbitration. Ultimately a majority of the US Supreme Court held that the arbitrators had exceeded their authority. Rightly or wrong, the Court, divided sharply along political lines, found that the arbitral tribunal’s interpretation of the parties’ agreement followed personal policy views rather than the proper contours of the applicable arbitration law.⁴³

III. Adjusting the Contract

A. Good Faith, ‘Abus de Droit’, ‘Treu und Glauben’

One little-explored area in which to examine the divergence between judge and arbitrator relates to provisions of national law that permit adjustment of the contract,⁴⁴ most notably on a

⁴¹ *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 130 S. Ct. 1758 (2010).

⁴² Under Rule 23 of the Federal Rules of Civil Procedure, a small number of plaintiffs is “certified” to represent a larger class of plaintiffs who have substantially similar claims, whether or not all members of the class participate in the matter.

⁴³ Some commentators consider that the Court, in its zeal to send a signal on the problematic nature of class arbitration, conflated the monitoring of arbitral jurisdiction (for courts) and deciding substantive merits of the parties’ dispute (for the arbitrators), giving the right answer to the wrong question. The relevant inquiry facing the Court was not, “What did the parties agree in general?” but the more limited issue, “What did the parties agree to arbitrate?” See William W. Park, ‘*La jurisprudence américaine en matière de class arbitration: entre débat politique et technique juridique*’, *Revue de l’arbitrage*, 3, 2012, page 507.

⁴⁴ For a comprehensive *tour d’horizon* of contract adjustment, see Joachim G. Frick, *Arbitration and Complex International Contracts* (Zürich 2001), Part III (at 145-226), addressing in particular the matter of ‘gap filling’ in complex agreements, adaptation clauses, the duty to renegotiate, an arbitrator’s power to adjust contract terms, notions of ‘changed circumstances’

theory such as ‘good faith’ and ‘abuse of rights’ (as in Switzerland)⁴⁵ or notions such as *Treu und Glauben* (in Germany),⁴⁶ *force majeure* and *imprévision* (in France).⁴⁷ National legal systems speak of other notions such as impracticability, frustration and impossibility (in common law systems),⁴⁸ *excessiva onerosità* (in Italy)⁴⁹ and/or *Wegfall der Geschäftsgrundlage*.⁵⁰

Sometimes a duty to renegotiate might arguably exist under principles of international trade law (sometimes called *lex mercatoria*) in the case of substantial upheaval (*bouleversement*)

and *lex mercatoria* derived from arbitral awards. See also Nagla Nassan, *Sanctity of Contract Revisited: A Study in the Theory and Practice of Long Term International Commercial Transactions* (1995).

⁴⁵ Article 2 of Swiss *Code civil*. Compare to Article 1134(3) of French *Code civil*, which speaks of abuse of contracts (*conventions*) rather than rights (*droits*), derived from the notion that contracts must be executed in good faith.

⁴⁶ German Civil Code (ZPO) in Section 162(2) provides *inter alia*, “If the satisfaction of a condition is brought about in bad faith by the party to whose advantage it would be, the condition is deemed not to have been satisfied.” (“*Wird der Eintritt der Bedingung von der Partei, zu deren Vorteil er gereicht, wider Treu und Glauben herbeigeführt, so gilt der Eintritt als nicht erfolgt.*”) See also Article 242, concerning the obligator’s duty to perform obligations according to the requirements of good faith, taking into account custom and practice.

⁴⁷ See e.g., French *Code civil* Article 1148 (*force majeure* as a defense to performance) and Article 1134(3), discussed *supra*, concerning the duty to execute contracts in good faith.

⁴⁸ See e.g., Uniform Commercial Code Article 2-615 (relieving performance made impracticable by an occurrence whose non-occurrence was a basic assumption of the contract) and Chitty on Contracts (31st Ed. 2012), Chapter 23 (Discharge by Frustration).

⁴⁹ Italian Codice Civile, Articles 1467-68.

⁵⁰ See e.g., German *Bürgerliches Gesetzbuch* Article 275 (no claim for performance of an act which is impossible (*unmöglich*). Analogously, Article 79 of the Convention on International Sales of Goods dispenses with liability when failure of performance was due to “an impediment beyond [the non-performing party’s] control” which could not reasonably be expected to have taken into account at the time of contract conclusion. International lawyers often speak of *rebus sic stantibus*. See Article 62, Vienna Convention on Law of Treaties, which addresses “Fundamental Change of Circumstances” and makes provision of a change whose effect is to “radically transform the extent of the obligations still to be performed under the treaty.” See generally, Detlev Vagts, ‘Rebus Revisited: Changed Circumstances in Treaty Law’, *Columbia Journal of Transnational Law*, 43, 2005, page 459.

in the economic equilibrium between the two sides.⁵¹ Such principles may be found in narrow usages within a specific industry, or broader trade usages that have been incorporated into the UNIDROIT Principles promulgated by the Rome-based “International Institute for the Unification of Private Law,”⁵² which attempt to suggest how commercial parties should react to dramatic and unforeseen circumstances that interfere with the performance of contract duties, either through excuse of performance, adaptation of the contract obligation, or a duty to renegotiate, failing which the contract terminates.⁵³

Judicial and arbitral attitudes need not diverge in applying such principles of good faith and abuse of rights. In some instances, different outcomes will result from a divergence in the decision-maker’s individual evaluation of the way changed circumstances should be addressed, regardless of whether the decision-maker is a judge or an arbitrator.

Such differences should not seem odd, given that they occur equally within a single legal system, particularly through legal principles allowing adjustment of contract through ‘filling the

⁵¹ These principles may be invoked both on the basis of industry custom, for example as provided in French *Code civil* Article 1135 and ‘commercial usage’ (*des usages du commerce*) in Article 1511 of the French *Code de procédure civile* as applied to international arbitration. Compare Articles 1135 and 1511 with Article 21 of the International Chamber of Commerce Arbitration Rules (2012 Version), stipulating that the tribunal “shall take account of ... any relevant trade usages.”

⁵² Principles of International Commercial Contracts, issued first in 1994, then re-issued with modifications in 2004 and 2010. See also Commission on European Contract Law (‘Lando Principles’) chaired by Danish law Professor Ole Lando, presented in full in 1998.

⁵³ The UNIDROIT Principles contain a section on ‘Hardship’ defined to exist when events fundamentally alters the equilibrium of the contract because the cost of performance has increased or the value received has diminished. The concept of hardship includes (*inter alia*) events that could not reasonably have been taken into account at the time of conclusion of the contract and whose risk was not assumed by the party. In the event of hardship the party may request renegotiation. On failure to reach an agreement a court may either (i) terminate the contract or (ii) “adapt the contract with a view to restoring its equilibrium.” See UNIDROIT Principles, Articles 6.2.2 and 6.2.3.

gaps' on matters the parties did not initially consider. A case decided in 1935 by the highest court in Switzerland involved hydroelectric power sold by the commune of Zermatt to the Gornergrat Railroad.⁵⁴ In 1895, a long-term concession for hydroelectric power had been granted to the railroad by the local municipality, or *Gemeinde*.

Decades later, a question arose as to what should be done with surplus power, a matter left open when the contract was concluded. The Swiss federal and cantonal courts came to the conclusion that a judge could in essence create a new contract term, thereby permitting sale outside the territory of the municipality. However, the federal court disagreed sharply with the cantonal court on the specificity to be used in filling the gap, insisting on coming up with calculations based on kilowatt hours.

Legal provisions that excuse performance or mandate adjustment of terms overlap with, but remain distinct from, provisions that permit arbitrators to disregard the strict rigors of otherwise applicable law on explicit authorization from the parties.⁵⁵ Notions such as *amiable composition* describe a process whereby arbitrators temper legal rules whose application violates what seems right in the circumstances, for example due to substantial completion of a project, or

⁵⁴ Gornergratbahn-Gesellschaft gegen Munizipal- und Burgergemeinde Zermatt, decision of 21 March 1935 in ATF 61 I 65 – 79. Review by the *Tribunal fédéral (Bundesgericht)* of a decision by the cantonal court in Valais concerning the 99-year concession. Thanks to Michael Schneider for background on this case.

⁵⁵ See e.g., French Code de Procédure Civile, Article 1512, authorizing *amiable composition* in international arbitration if provided by the parties' agreement. For international contracts, references to *amiable composition* may assume less precise contours than provided under French law, a bit as 'due process' has come to be used in arbitration without necessarily drawing its significance from U.S. law. French Code de Procédure Civile Article 1478 contains similar principles authorizing decision in *amiable composition* for domestic arbitration.

unexpected exchange rate modification.⁵⁶ Rather than aiming at legal accuracy, the arbitrator reaches toward general notions of ‘right’ encrusted with emotional overtones and sometimes in tension with court decisions, statutes or strict contract terms.

A long-standing debate surrounds whether *amiable composition* amounts to the same thing as decision-making *ex aequo et bono*, according to the ‘right and good’.⁵⁷ While the notions are often used interchangeably, they may not be coextensive. Arbitrators who decide *ex aequo et bono* might begin and end with a private sense of justice, going directly to a personal view of the right result, while in *amiable composition* the arbitrators would start at rules of law, departing only if needed to achieve a just result.⁵⁸ The difference is significant, given that there is nothing inherently unjust about most norms of commercial law.⁵⁹

⁵⁶ See Eric Loquin, *L’amiable composition en droit comparé et international: Contribution à l’étude du non-droit dans l’arbitrage commercial* (1980). See also, W. L. Craig, W. W. Park & J. Paulsson, *ICC Arbitration* (3rd Ed., 2000), §§3.05 at 110-114.

⁵⁷ The Arbitration Rules of the International Chamber of Commerce (in Article 21(3) of the 2012 Rules) mention both *amiable composition* and *ex aequo et bono*, saying that a tribunal may (if authorized) “assume the powers of an amiable compositeur” or “decide *ex aequo et bono*.” The French version follows similar structure, with the disjunctive “or” leaving two distinct notions, as in “law or equity.” The disjunctive “or” may suggest the notions remain separate, or may simply suggest different ways to express similar concepts. The Rules permit *amiable composition* and *ex aequo et bono* decision-making only if agreed by the parties. In accord with that principle, see Richard M. Mosk, ‘Arbitrators Should Apply the Law’, *Los Angeles Daily Journal* (19 April 2011) urging *ex aequo* decisions only with the express consent of the parties.

⁵⁸ Compare Philippe Fouchard, Emmanuel Gaillard, & Berthold Goldman, *Traité de l’arbitrage commercial international* (1996), Section 1502 at 836-37. The authors seem to admit the option either to proceed directly to justice or first to consider the applicable law. Nevertheless, they suggest that such a nuance lacks significance (“*une telle distinction ... paraît artificielle*”) because the arbitrators can always do what they think justice requires.

⁵⁹ The meaning and availability of such principles remain distinct from the question of whether it would be wise for contracting parties to agree to such flexibility. With respect to the substance of many economic transactions, such as a seller’s right to be paid or the insured’s right to be reimbursed, the slim objective content of notions such as fairness may make the concept problematic. Legal rules permit individuals, companies and governments to evaluate risks and make choices. Imagine an arbitrator hearing claims against a banker who wrongfully refused to

B. Modification Pursuant to Contract: Gas Price Adjustment

An intriguing comparison between judge and arbitrator might be found in adjustment of agreements pursuant to explicit contract terms, rather than a legal rule such as those cited above related to good faith or abuse of rights. National law would enter the picture through the side door of an overarching applicable law clause, providing for contract interpretation according to principles found in the legal system of some ‘third country’ not that of either side to the contract, perceived as neutral between the parties (a traditional role for Swiss law) or perhaps especially developed in the substance of the contract (such as English law for maritime matter).

Such arrangements can be found in price adjustment arbitrations related to long-term natural gas supply.⁶⁰ The gas supply agreements attempt to provide a mechanism to address dramatic economic upheaval by permitting price adjustment for substantially changed circumstances.⁶¹ The contract might allow arbitrators to create a new price formula in light of

return the entirety of a customer’s funds. “My deposit was \$1,500,” says the customer. “Ah, yes,” replies the banker. “But such dreary historical facts must yield to moral concerns for balance, symmetry and charity. We have rounded your account down to \$1,000 and transferred the balance to a most deserving charity.”

⁶⁰ For a general description of the process, see e.g., Ben Holland & Phillip Spencer Ashley, ‘Natural Gas Price Reviews: Past, Present and Future’, *Journal of Energy, Natural Resources & Environmental Law*, 30 (No. 1), 2012, page 29; Marwan M. A. Musleh, ‘Pacta Sunt Servanda in Gas Price Reviews’, presentation at International Bar Association, Boston, 9 October 2013. See also Richard Power, Gas price reviews: is arbitration the problem? *Global Arbitration Review* 8 March 2014. Admitting the difficulty of any safe conclusion without seeing the agreements at issue in recent price adjustment arbitrations, the author nevertheless speculates that arbitrators may be abandoning proper contract construction, departing from links to oil prices in favor of gas spot prices.

⁶¹ The adjustment clause might provide with a provision saying that arbitrators can review the Price Formula (usually a complex equation based on some index of energy values, already fixed in the agreement) to see whether that formula “needs to be revised to reflect significant changes in the buyer’s energy market which affect the value of gas in the buyer’s end user market, as such value can be obtained by a prudent and efficient gas company.” If the formula does need to be revised, its modification might be mandated so as to “allow the Buyer to market the gas

changes affecting the value of gas obtained by a ‘prudent’ gas company so as to let the buyer market the gas ‘economically.’⁶²

Such adjustment clauses attempt to give contours to the ‘when, why and how’ of adjustment. The contract provisions aim to provide more specificity than the notion of *pacta sunt servanda* (‘agreements are to be kept’)⁶³ borrowed from public international law, but interpreted in conjunction with the corollary principle *clausula rebus sic stantibus*, to the effect that the agreement is binding ‘so long as things stand as they are.’⁶⁴

On closer reflection, however, such price adjustment clauses may prove more malleable than initially expected, particularly if the buyer’s profit margin is considered.⁶⁵ Does marketing ‘economically’ mean to sell in a way that is ‘stingy’ and cheap? Or to market in a way that is economically sound? Either meaning might fit.

Such price adjustment contracts will be subject to some applicable law, such as the law of England, Switzerland or New York. Perhaps that law will have something to say about how the

economically” (or “commercially” in some instances) under the assumption of “sound marketing practices by prudent and efficient operations on the part of Buyer.”

⁶² For an instance when such a decision was challenged for excess of powers under Section 10 of the Federal Arbitration Act, see *Gas Natural Aproveisionamientos v. Atlantic LNG of Trinidad Tobago*, 2008 WL 4344525 (S.D.N.Y. 2008).

⁶³ The essence of the concept appears in Justinian’s Code II.3.29 (chapter De Pactis): *sancimus nemini licere adversus pacta sua venire et contrahentem decipere* (“we shall not allow anyone to contravene his agreements and thereby disappoint (deceive) his contractor”).

⁶⁴ See e.g., Ian Brownlie, *Principles of Public International Law* (6th ed. 2003), at 591-92. The corollary, of course, is that treaties are binding “so long as things stand as they are” (the so-called *clausula rebus sic stantibus*). See generally, J. L. Brierly, *The Law of Nations* (1963), 317-345; F. A. Mann, *Studies in International Law* (1973), 327-359.

⁶⁵ Thus some observers challenge the utility of the notions ‘*pacta sunt servanda*’ (contracts to be performed) and its corollary ‘*rebus sic stantibus*’ (assuming things remain the same), suggesting that they are too broad and general to be helpful in practice.

controverted words should be interpreted. In many instances, however, the choice of law clause, for an international arbitrator, will prove less useful than hoped.

To explore why the law has its limits, one might recollect the old Latin maxim *noscitur a sociis* ('a word is known by the company it keeps'). Context dictates meaning, with words taking a different sense from divergent sentences. Our feet run. Our noses run. One might see a run on the bank.⁶⁶

So the problem with national law as an interpretative tool (whether statute or case law) is that controverted terms arise in a domestic context different from the international circumstances facing the arbitrator. What is a 'prudent' gas company? The 'prudent' standard in national law might derive from cases regarding utility rates,⁶⁷ determining fiduciary obligations for trustees, or making damage calculations in light of a duty to mitigate.⁶⁸

The quintessentially national context of most law can make national standards less than ideal for interpreting international agreements. For better or for worse, however, the arbitrator cannot just give up and say, "This is too hard for me!" Often, a search for the one good approach may need to be replaced by an identification of wrong paths to avoid. However, as Rudyard Kipling might have written, that is a story for another day.

⁶⁶ Linguists sometimes describe phenomenon by word 'polysemy'. If someone says "I get it" this might mean "I understand" or "I receive it" or "I buy it" or "I catch a disease."

⁶⁷ Texas Public Utility Commission, Application of El Paso Electric Company for Authority to Change Rates, 10 Tex. P.U.C. Bull. 1071, 1984 WL 274081 (Tex.P.U.C.) (Dec. 7, 1984)

⁶⁸ For example, New York courts have said that an injured party who makes an effort to avoid or reduce damages may be allowed to recover related expenses if the effort was made, *inter alia*, prudently and efficiently. *Den Norske Ameriekalinje Actiesselskabet v. Sun Printing & Publishing Ass'n*, 122 N.E. 463 (Mar. 4, 1919). Even in oil and gas leases, the word 'prudent' might change from one context to another, whether the operator's drilling decisions, production operations, or marketing. See e.g., Gary B. Conine, 'The Prudent Operator Standard: Applications beyond the Oil and Gas Lease', *Natural Resources Journal*, 41, 2001, page 23.

IV. More Shades of Gray: Choice of Law and Transnational Norms

Choice of law problems pose special challenges for arbitral interpretation. National judges understandably take their starting point in the private international law principles of the forum. However, an international arbitrator will often need to look elsewhere, since questions of applicable law often arise precisely because there is no obvious indication of which legal system (or systems) should govern the controverted question.

The task becomes particularly vexing in deciding whether a non-signatory should be bound by an arbitration agreement on the basis of some contract theory.⁶⁹ When doubt has been raised about who agreed to arbitrate, arbitrators can face a ‘chicken and egg’ conundrum. The side arguing that an agreement exists might urge application of the governing law designated by the contract itself, even though that law was clearly not intended to govern relationships with strangers. In some instances, the right answer may depend on whether a signatory to an arbitration agreement seeks to enforce it against a non-signatory defendant, or whether an arguable outsider (the non-signatory) moves to compel arbitration against a signatory who has clearly agreed to arbitrate with a corporate affiliate of the claimant.⁷⁰

⁶⁹ One well-known American case presented a litany of five theories for binding non-signatories: (i) incorporation by reference; (ii) assumption; (ii) agency; (iv) veil-piercing/alter ego; and (v) *estoppel*. Under the facts of the case, the court rejected each theory as insufficient to bind Thomson to the arbitration agreement of its subsidiary. See *Thomson-CSF, S.A. v. American Arbitration Ass’n*, 64 F.3d 773, 776 (2d Cir 1995). For a recent discussion of the agency theory in American jurisprudence, see *Covington v. Aban Offshore Ltd.*, 650 F.3d 556 (5th Cir. Tex. 2011). See generally William W. Park, ‘Non-signatories and International Contracts: An Arbitrator’s Dilemma’, in *Multiple Party Actions in International Arbitration* 3 (PCA, 2009); William W. Park, ‘Rules and Standards in Private International Law’, *Arbitration*, 73, 2007, page 441.

⁷⁰ See also *Fluor Daniel Intercontinental, Inc. v. GE.*, No. 98-Civ. 7181 (WHP), 1999 WL 637236 (S.D.N.Y. 1999) where *estoppel* permitted a non-signatory respondent to benefit from an arbitration clause signed by a subsidiary.

If a claimant wants to join to the arbitration an unwilling respondent on the basis of having agreed to arbitrate through a *de facto* or ostensible agency, the national judge will look to his or her *lex fori* for principles that suggest either when an agency might be found, or when a foreign law or agency should be taken into account.⁷¹ By contrast, a thoughtful arbitrator might find it difficult to determine agency by looking to the applicable law designated by the contract, or even the arbitral *situs*.

If indeed the unwilling non-signatory respondent proves to be a stranger to the contract, then that person would not have agreed to either arbitration or the contract's governing law. In such circumstances, an arbitrator who starts with the contract's designated law risks presuming the conclusion, essentially pre-judging the question by taking the non-signatory as connected enough to come within the contractually-designated law, when as a matter of logic that is the precise point open to debate.⁷² Tempting as it may be to simplify the decision-making process by looking to the contract, since that approach would treat the non-signatory *a priori* as having consented to application of the contract before that determination was in fact made.

The point often escapes some of the sharpest thinkers, usually because of a tendency to assume that legal systems converge in their rules on agency, which of course represents another form of presuming the conclusion. If legal systems do not differ, then of course the choice of law problem does not arise. However, the need for some extra-contractual starting point becomes

⁷¹ Compare the French and British decisions in *Dallah Real Estate & Tourism Holding Co. v. Ministry of Religious Affairs, Gov't of Pakistan*: [2010] UKSC 46 and Cour d'appel [CA] de Paris, Case No. 09-28533, Feb. 17, 2011. Article V(1)(a) of the New York Convention states that a recognition and enforcement of the award may be refused if the arbitration agreement "is not valid under the law to which the parties have subjected it or of the country where the award was made."

⁷² Of course, the arbitrator might be quite sensitive to the law of the arbitral seat (and/or the place of enforcement) given the natural inclination to safeguard the award from annulment or non-recognition.

more vivid on positing a real conflict, with sharply differing legal systems. Imagine that chosen law of the contract, let us say the law of Ruritania, provides that wives and girlfriends will be bound by contracts concluded by their husbands and lovers. If the man in the relationship concludes a loan subject to the law of Ruritania, does that mean the woman will be bound to pay the debt, as well as to submit to arbitration on the matter? The question, of course, should be rhetorical.

In consequence, arbitrators may base decisions about such matters on ‘transnational norms’ which become applicable through the practice of arbitral proceedings as well as so-called ‘general principles of law.’⁷³ Although such transnational norms might well derive from what French scholars term ‘*un ordre juridique arbitral autonome*,’⁷⁴ the arbitrator often seeks to apply transnational norms not for reasons of ideology, but simply as a practical starting point for analysis in the absence of clearly applicable national law.

V. Conclusion

Do arbitrators apply national law differently from judges? The answer, unsatisfying to ideologues, and those hesitant to embrace uncertainty, must be ‘sometimes.’

Although generalizations remain risky, judges and arbitrators diverge not so much due to any personality change that overcomes an individual wearing judicial robes, but rather from variations in the respective starting points for decision-making authority. Different departure

⁷³ See *Rhône Méditerranée v. Achille Lauro*, 712 F. 2d 50 (3d Cir. 1983), validating an arbitration clause that contravened a provision of Italian law calling for an odd number of arbitrators even if the clause made provision for an umpire tie breaker. The court held that a commitment to arbitrate would be deemed “null and void” under the New York Convention only if defective by reason of “an internationally recognized defense such as duress, mistake, fraud, or waiver” or when contrary to some fundamental policy of the forum state.

⁷⁴ Emmanuel Gaillard, *Aspects philosophiques de l’arbitrage international* (2008).

points may yield different results, particularly with respect to contract terms that might appear at odds with applicable law. Judges normally take power from the political collectivity that makes their appointments and pays their salaries,⁷⁵ whereas the arbitrator's authority lies in an agreement to waive jurisdiction of otherwise competent courts.

In an international contract, the primacy of the parties' agreement may lead arbitrators to conclude that the litigants intended to invoke only part of a national legal system. By contrast, a judge may feel inclined to apply more broadly the norms of his or her own state, perhaps tweaked by an impulse to shape those norms to reflect the forum's changing policy concerns.

Thus arbitrators may sometimes show greater fidelity to the established rule of a chosen law, foregoing any policy-making function similar to that sometimes asserted by common law judges. In adjusting international contracts, arbitrators face special tensions in their search for equilibrium between rival notions of predictability, often expressed in imprecise terms like 'commercial reality' or 'strict letter of the law' which like the humble chameleon take different colors depending on the backdrop. The ultimate stakes lie in arbitration's ability to fill its promise in promoting the type of economic cooperation enhanced by reliable vindication of legitimate expectations. In the search for balance, common sense will likely pay far more dividends than ideology.

⁷⁵ Even when judges look to court-selection clauses as the source of adjudicatory jurisdiction, such provisions must be given effect through the lens of the forum's procedural law.