Chapter 2: Effect of International Public Policy in International Arbitration

Pierre Mayer

I. Introduction

2-1 It is first necessary to clear up the ambiguity of the expression: international public policy.

2-2 In civil law countries, the expression “ordre public international” means: the concept of public policy as applied in private international law. It is in fact the limited part of the public policy of a State which may constitute an obstacle to the application of a foreign law by the courts of that State, or to the recognition of a foreign judgment or arbitral award by such courts. It is in that sense that the expression is used in the “Resolution on public policy as a bar to the recognition of international arbitral awards” adopted in New Delhi in 2002 by the ILA (International Law Association).(1)

2-3 In a second sense, international public policy is the part of public policy which belongs to public international law. As an example, an embargo decreed as a sanction against a State by the Security Council of the United Nations(2) belongs to international public policy in that sense. To avoid any confusion with international public policy as a device used in private international law, it is sometimes called “truly international public policy”.

2-4 That leads me to distinguish truly international public policy from a third notion: that of transnational public policy, although unfortunately the two expressions are sometimes considered as synonymous. Transnational public policy in international arbitration is in fact the subject of my presentation, as I guess from the examples which are given as illustrations in the programme.

2-5 I shall successively consider:

• First, the notion of transnational public policy
• Secondly, its nature
• Thirdly, as a link with the subject addressed by Donald Donovan, the question whether, in a given case, an arbitrator should choose to rely on transnational public policy or rather to apply the mandatory rules of a State – the result being most often the same.

II. Notion of Transnational Public Policy
2-6 “Transnational public policy” can be defined as the set of legal principles, not belonging to the law of a particular State, which may be relied upon by an arbitrator either as a bar to the enforcement of an international commercial contract, or, in a less direct manner, as an obstacle to the application of the State law normally applicable to such contract. The concept was introduced by Pierre Lalive in his famous report at ICCA in New York in 1986, and is now a classic.\(^{(3)}\)

2-7 Indeed, transnational public policy is a necessary device in international arbitration. Since, unlike a court, an international arbitrator is not an organ of a State – even the State where he sits – it is neither easy nor satisfactory for him to rely on the public policy of any given State. He needs to have his own public policy.

2-8 On what is it based? A succinct answer to that question was given by the Institut de droit international at its session of Santiago de Compostela in 1989. A Resolution was adopted, pursuant to which in no case shall an arbitrator violate principles of international public policy as to which a broad consensus has emerged in the international community.\(^{(4)}\)

2-9 Evidence of such a consensus will most often result from a scrutiny of the legal systems of the various States, or from the existence of one or more international treaties. A typical example of the way arbitrators reason is the famous award rendered by Judge Lagergren in a case in which a party claimed the payment of a commission, which in the circumstances clearly appeared to have been promised as a reward for acts of corruption. Although the defendant only raised objections based on the interpretation of the contract, the arbitrator invoked transnational public policy to justify its refusal to even enter into the merits of the case:

> Such corruption is an international evil; it is contrary to good morals and to an international public policy common to the community of nations.\(^{(5)}\)

2-10 Other principles often cited by authors are those which condemn:

- racial or religious discrimination
- drug trafficking
- terrorism
- trade in stolen art objects
- traffic in human organs.

2-11 The notion of transnational public policy thus appears relatively clear; its nature is more ambiguous.

**III. Nature of Transnational Public Policy**

1. **Proposed Analysis**

2-12 Transnational public policy performs the same function as State public policy or truly international public policy: it eliminates the agreements, rules or decisions that would contravene certain fundamental values or interests. But does it have the same nature? When we say, for instance, French public policy, or English public policy, we refer to a component of a given legal system. That legal system imposes on its subjects the duty to
comply with the principles and rules on which it confers a public policy character, and in case of non-compliance it imposes on its courts the duty to restore a situation that will be in accordance with these principles and rules. Similarly, truly international public policy is a part of international law, the part which even an agreement between two States may not violate. Can the same be said of transnational public policy? Is there a legal system, distinct from the States and from international law, that imposes on its subjects the duty to respect the principles and rules on which it confers a public policy character?

2-13 Such a legal system has been said to exist. One of its finders, or inventors, Professor Berthold Goldman, has given it the name of *lex mercatoria*. Others prefer to call it new law merchant, or transnational law, although this last expression has also been given other meanings, notably by Professor Philip Jessup. *Lex mercatoria* would be the legal system spontaneously emerging from the society of international merchants, the so-called *societas mercatorum: ubi societas, ibi jus*. And transnational public policy would be the part of the *lex mercatoria* presenting the characters of public policy.

2-14 It is important to decide whether transnational public policy is, or is not, a part of a legal system, because its nature will not be exactly the same.

2-15 I personally do not believe that a legal system corresponding to the definition of *lex mercatoria* exists. Since this is not the time and place for a demonstration, I shall just mention briefly the main reason why I think that *lex mercatoria* may well be the name given to a set of legal rules, but does not constitute a legal system.

2-16 A legal system is formed not only of rules, but, even more importantly, of judges and of organs exercising a power of coercion. *Lex mercatoria* lacks both. In particular, contrary to what has been suggested by some authors, arbitrators are not empowered to adjudicate disputes by the society of merchants and do not render their awards in the name of that society: they receive their powers only from the parties in the particular dispute; and only State courts and State organs of coercion are able to enforce arbitral awards. It is even doubtful that there is a society of international merchants; it requires more than doing business together to form a society.

2-17 Now, even if there was a society of international merchants, could the principles known as transnational public policy emanate from that society? This would be surprising, since what these principles accomplish is mainly to limit the freedom of trade, which is not what merchants normally wish to do. If we take for instance the prohibition of the traffic of illicit drugs, there are on the one hand those who are involved in such trafficking, who do not want it to be limited, and on the other hand those whose activities are totally different, who simply do not care; or if they do, it is as ordinary citizens, not as merchants.

2-18 The prohibition, as an element of transnational public policy, therefore rests on the common feelings of ordinary citizens, inscribed in the legislation of a majority of States, and/or in international treaties drafted and signed by them. That does not make it part of a legal system which would be distinct both from the States and from international law.

2-19 What is transnational public policy then? And since it is not a set of legal principles having a binding force, resting on a legal system, where does its power to deprive a contract of its binding
force, or to exclude the law chosen by the parties, come from? What justifies that an arbitrator, who is supposed to order the parties to abide by the terms of their agreement, refuses to do so on the ground that these terms violate a principle which he declares to be part of transnational public policy?

2-20 There is in my opinion only one possible answer to such question, although it may seem disappointing: it is his position as an arbitrator that gives him the freedom to invoke the principles which he considers to be worthy of being respected. Transnational public policy is not imposed on the arbitrator, it is imposed by the arbitrator, by virtue of the powers conferred on him by the parties.

2-21 Let me immediately qualify this statement. I am not saying that the arbitrator is at liberty to do anything he pleases. He should act reasonably, he should defend, and defend only, those principles which are considered as inviolable by the community of men, or by a majority of States having enacted legislation or entered into treaties in order to protect them. That is his duty, it being observed that it is not a legal duty since it is not sanctioned as such; it is a professional, and to some extent a moral, duty.\(^{(10)}\)

2. Consequences of the Proposed Analysis

2-22 This approach leads to slightly different results from those to which one is led if one considers transnational public policy as an objective element of a transnational legal order. In the approach which I favour, the arbitrator's duty is less strictly defined. He enjoys a certain degree of liberty in his assessment of what is tolerable and what is not.

2-23 When one mentions the necessity of a consensus between States, how broad must the consensus be? It is for the arbitrator to decide. When one insists that, to be part of transnational public policy, a principle must be of paramount importance, who assesses the importance of a given principle? It can only be the arbitrator. There is no absolute truth: one arbitrator may consider that a certain principle, which is shared by a majority of States, but rejected by an important minority, does not deserve to be upheld, to the detriment of the party who claims that the contract must be performed. Another arbitrator may take the opposite view. Their respective moral and even religious convictions play a role.

2-24 There is a famous case which illustrates that rather clearly: the case of the ship “Le Créole”. It was a slave ship which carried slaves belonging to American owners. The slaves revolted while the ship was at sea, and sailed it to the Bahamas. When they arrived, the English authorities set them free, slavery having been abolished in England. The United States espoused the claim of their nationals, and a mixed arbitral commission had to decide whether England, by setting the slaves free, had violated international law.

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2-25 The award was rendered in 1855. It reads:

\[\text{I do not need to cite authorities to demonstrate that slavery, although odious and contrary to principles of justice and humanity, can be established by the laws of a country; and that, having been so established in several countries, it cannot be against the law of nations.}\(^{(11)}\)\]
2-26 The award, deciding a case between two States in accordance with international law, may have been correct at the time. But suppose the dispute had been brought before you, as an arbitrator, by the owners claiming that their title be recognised and the slaves returned to them, would you, even at the time, have counted how many States had established slavery, how many ignored the institution and how many condemned it? I suppose not. You would have relied on the fact that slavery is "odious and contrary to principles of justice and humanity", because you would have shared these principles.

2-27 Transnational public policy is not a definite part of a legal system, which the arbitrator would have the duty to uphold; it is a device which allows the arbitrator to refuse to enforce a contract, or to apply a law, which contravenes values which he, in accordance with a view shared by the community of men and endorsed by legislators (national or international), deems to be essential.

IV. Choice between Reliance on Transnational Public Policy and Application of Mandatory State Rules

2-28 Since transnational public policy must reflect a broad consensus between the States, in most cases it will not differ from the rules which are to be found in the applicable State law. Is it then preferable to apply the mandatory rules of the State, or to invoke transnational public policy?

2-29 I shall distinguish two situations, depending on whether the mandatory State rule is present in the *lex contractus*, or is only present, as a *loi de police*, in the law of another State, not chosen as *lex contractus* by the parties.

2-30 In the first situation I do not see why the arbitrator would not simply apply the *lex contractus*. A precise rule is preferable to a vague principle. In addition, if the *lex contractus* has been chosen by the parties it would even be strange not to apply it without a major reason.

2-31 In the second situation it is more difficult to choose. The choice is between reliance on transnational public policy on the one hand, and on the other hand the *méthode des lois de police*, consisting of the application of a law other than the *lex contractus*, based on its mandatory character and on its close connection with the situation. (12)

2-32 The second reasoning was adopted in an ICC arbitration award in 1989. A contract had been concluded between a Hungarian company and a foreign company, for the collection and sale by the first party to the second, of certain glands to be taken from dead human bodies in Hungary. The contract was subject to Swiss law. It was argued by the buyer that the contract violated the principle of the integrity of the human body. The arbitral tribunal checked whether under Hungarian law – as the law of the territory – such trade was licit or not; it found that it was licit. (13)

2-33 If the tribunal had chosen to rely on transnational public policy, it would not have found a precise answer to the problem because the scope of the prohibition of the trade of human organs varies: in some countries the prohibition is absolute, while in other countries it depends on whether there is a payment, or even on who pays whom. It is preferable to apply the precise rules of the State concerned, rather than a vague principle which is not applied in the same manner in the various countries.
2-34 The same can be said of the prohibition of corruption. Where there is a clear act of corruption, which is proven, the easy way, it is true, to apply the transnational public policy principle. But the limit is not always clear between what is licit commission and what is corruption. For instance in some countries one has to distinguish between innocent “facilitating payments” and corruption. Equally since it is most often impossible to prove the existence of corruption, there are sometimes legal provisions which prohibit the payment of any commission, based on a presumption of corruption. Such technical rules cannot be part of a transnational principle; however, it may be justified to apply them if they serve legitimate State interests.

2-35 Transnational public policy is a particularly convenient notion when the public policy principle is universally recognised, and where, at the same time, there is no doubt that it has been violated. When it is not universally recognised, much depends on the subjective views of the arbitrator; that cannot be avoided. Also, where the exact scope of the principle is uncertain, other mechanisms may have to be preferred. Transnational public policy therefore undoubtedly appears as one, but only one, of the devices which the international arbitrator may use to protect values which the parties are not allowed to ignore.

Professor at the University of Paris I (Panthéon-Sorbonne).

1 The text of the Resolution can be found in the Report of the New Delhi Conference and in xxix YBCA 339 (2004), with a presentation by Pierre Mayer and Audley Sheppard.

2 Such as the ones adopted against Iraq in 1990 and 1991.


4 The text of the Resolution can be found in 79 Revue critique de droit international privé 191 (1990).

5 Award rendered in ICC case no. 1110, Argentine engineer v. British company, 3 Arb Int 282 (1987). It has been partially published by Julian D M Lew, Applicable Law in International Commercial Arbitration (Oceana 1978), p 553. See also ICC case no 1110, ibid.


7 See Philip Jessup, Transnational Law (Yale University Press 1956).


9 See, for example, Philippe Fouchard, L’arbitrage commercial international (Dalloz 1965), 403, according to whom arbitrators and arbitral institutions are the “veritable prevoir jurisdionnel de [la] société internationale des commerçants”.


13 ICC Award no 5617, extracts in 121 Journal du droit international (Clunet) 1041 (1994).