

Mandatory Rules and Public Policy as Limitations on the Applicable Law in International Arbitration

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SUMMARY

The article examines the concepts of mandatory rules and public policy as limitations on party autonomy in the arbitral context. It highlights the differences between their application in international litigation and international arbitration, and considers the different bases for their application. It concludes that the mandatory rules that often find application in international litigation are not a given in international arbitration. In relation to application of the mandatory rules of the proper law, the article provides the context in which these mandatory rules could apply, namely, after a consideration of the wording of the choice-of-law clause. As to application of the mandatory rules of a third country, the article provides the reasoning on which the laws of third countries should be taken into consideration, but concludes that the mandatory rules most likely to find application, in this context, would be the law of the place of enforcement. Application of the mandatory rules of the arbitral seat is also considered. In this context, the article considers the overlap between the arbitrability of an issue and the mandatory rules. The article proposes, subject to the nature of the mandatory rules, that the mandatory rules of the arbitral seat may be taken into consideration. The consideration of their nature revolves predominantly around public-policy grounds. The point is made that the place where the arbitral proceedings are held (the place of enforcement of the agreement) affords the arbitral legal order the space and regulatory framework in which to conduct the arbitration, and its rules should therefore be respected. The place where an application is made in order for an arbitral award to be set aside is also usually the place of the legal seat of the arbitration. Both instances, therefore, refer to only one legal system. The only other legal system of potential applicability is the law of the place of enforcement.

KEYWORDS: international arbitration, applicable law, private international law, mandatory rules

1 INTRODUCTION

International arbitration is based on the principle of party autonomy. The choices that parties can exercise in arbitration give rise to complexities that do not present themselves in litigation proceedings. While it is true that the laws of the same states would compete for application, the reasoning for their application in arbitration would differ from their application in litigation. The questions that arise in this context would seem neatly to meet the intersection between theory and practice, once more giving rise to old questions of the loyalties owed to the sovereign. It is well known that mandatory rules and public policy function as a limitation on party autonomy. The choice-of-law questions that arise in this context can be considered against a backdrop of the semi-autonomous nature of the arbitral legal order and its relationships with the community of states in which it functions.¹ There are limitations to the arbitral legal order in this context. Party autonomy alone cannot override the mandatory rules and public policy of states. The question is then to determine which states (and their legal orders) have an interest in limiting the autonomy of the parties. The problem is that if the arbitral legal order is considered to be independent of any state, the question becomes more complex than in instances where a court applies the mandatory rules. This is simply because a state court owes certain loyalties to the state from which it derives its authority. On the other hand, the arbitral tribunal derives its authority from the parties themselves, so the loyalties that are owed to a state (by an arbitral tribunal) are more limited. States would, however, naturally still have an interest in matters under certain circumstances (where a state's law was violated, or where performance took place there, or where a state is called upon to enforce an award). The viewpoint from which the matter should be approached is the consideration of whether a state has a legitimate interest in the matter that would allow its law to overrule the rules of law that the parties have themselves chosen. Article 9(2) of the Rome I Regulation,² which in many ways sets out the best practice on the law applicable to contractual obligations, is important in this determination. Article 9(1) states that mandatory rules are

“provisions, the respect for which is regarded as crucial by a country for safeguarding its public interest, such as its political, social or economic organisation, to such an extent that they are applicable to any situation within their scope, irrespective of the law otherwise applicable to the contract.”

The provision demonstrates that it is important that the provisions have a public interest at their heart, or that the provisions are necessary to protect a weaker party, such as consumers. The above will be used for guidance in determining which country's laws should possibly find application in the arbitration. There are, of course, rules of several states that could be considered in this case: the mandatory rules of the substantive law; the

¹ Adams “The Semi-Autonomy of the Arbitral Legal Order” 2020 16(2) *Asian International Arbitration Journal* 140 146–157.

² The European Parliament and the Council of the European Union *Regulation (EC) No 593/2008 on the Law Applicable to Contractual Obligations (Rome I)* (17 June 2008).

mandatory rules of the *situs*; the mandatory rules of a third state; or even the mandatory rules of the place/s of enforcement.

2 THE MANDATORY RULES OF THE LAW APPLICABLE TO THE CONTRACT

The mandatory rules of the substantive law (governing law of the contract) are discussed first. It would seem natural that the mandatory rules of the chosen law would apply, but the matter is more dependent on interpretation than would first meet the eye. When parties choose the law applicable to their agreement, are they merely choosing a *lex contractus* or are they choosing the entire legal system as being applicable to the agreement?³ The so-called Copernican Revolution in the conflict of laws occurred when Von Savigny re-theorised the private international system of law from its conception as a choice of specific rules, as was understood in the Statutist period, to one that comprised the choice of an entire legal system. Does this hold equally true in the case of arbitration?⁴ If the consideration is that private-international-law rules are not automatically applicable to the arbitration, then a choice of law by the parties would not necessarily include the entire legal system, but only the *lex contractus*. The drafting of the choice-of-law clause then becomes important in this matter, as the “mandatory rules” in this case are in fact subject to the choice made by the parties.⁵ For instance, consider the following clause: “The contract shall be governed in accordance with the law of State X.”⁶ This provision clearly encompasses only the application of the substantive law of the contract (the *lex contractus*), including within its scope the issues that one would generally consider to be part of the law of contract, such as performance and validity. However, in such a case, no mention is made of the mandatory rules of the chosen law, and so the interpretation that could be given to such a clause is that they have not been chosen and are therefore not applicable if they are not directly related to the law of contract. A choice-of-law clause stipulating that “this contract shall be governed by the law of State X” is likely to bear a similar interpretation insofar as its reference is only to the contractual law of the state concerned.⁷ This type of clause may, however, provide more ambiguity and may possibly be construed as choosing the entire legal system as being applicable. This would include the mandatory rules of that system, including issues such as competition law, trade control and

³ Nygh (*Autonomy in International Contracts* (1999) 230) expresses a similar idea in his discussion of the work of Derains and Mayer. For the latest authoritative discussion on mandatory rules in the context of the Covid-19 pandemic, see Neels and Fredericks “Covid-19 Regulations as Overriding Mandatory Provisions” in Watney et al (eds) *The Impact of Covid-19 on the Future of Law and Related Disciplines* (2022) 1–25.

⁴ See the discussion in Adams and Kruger “Private International Law and Choice of Law Clauses” in (eds) Hutchison and Myburgh *Research Handbook on International Commercial Contracts* (2020) 114–116 on the history of party autonomy, where, after the Statutist period, there was a change from the application of the singular rules of a legal system to the application of an entire legal system. See further Forsyth *Private International Law: The Modern Roman Dutch Law Including the Jurisdiction of the High Courts* (2012) 48–49.

⁵ Born *International Commercial Arbitration* (2020) 2707.

⁶ Born *International Commercial Arbitration* 2708.

⁷ *Ibid.*

intellectual property.⁸ The ambiguity created in these situations does not arise in the case of litigation, because it is automatically assumed in these cases that the governing law as a subject of private international law applies to all issues concerned – contractual or otherwise. This argumentation therefore leads one to conclude that the outcome of the applicable law would be different if the parties stipulated that the agreement was “governed by the law of Switzerland” or “articles X-Y of the Swiss Civil Code”.

If a non-state law were chosen as the governing law of the contract, what would the implications be for mandatory rules? Would the mandatory rules of the otherwise applicable law become relevant? It seems unlikely that the law that is most closely connected with the contract would then become applicable in such cases, as the law might not have any practical effect on the contract.⁹ The objective proper law of the contract should apply only if that state has an interest that needs to be protected. Cases where this may present itself are discussed below.

3 THE MANDATORY RULES OF A THIRD COUNTRY

Consideration often turns to whether there are any other mandatory rules that may find application. This may include the law of a third country (or another country) that is neither the substantive law of the contract nor the law of the forum.¹⁰ In litigation, there are two underlying theories as to why a court should consider the laws of a third country the first one calling for this application being the interest of the third country in having its law applied,¹¹ and the second stemming from the principle of comity.¹² If the arbitral legal order is accepted as a community that exists on the same plane as states, as far as its rules are concerned, then the likely conclusion is that it is bound

⁸ See Born *International Commercial Arbitration* for other examples of mandatory rules. Nygh (*Autonomy in International Contracts* 230) seems to take a similar position, stating that the parties may exclude mandatory rules by wording the choice-of-law clause appropriately.

⁹ See art 11 of the Hague Principles on Choice of Law in International Commercial Contracts (2015), which states: “These Principles shall not prevent an arbitral tribunal from applying or taking into account public policy (*ordre public*), or from applying or taking into account overriding mandatory provisions of a law other than the law chosen by the parties, if the arbitral tribunal is required or entitled to do so.”

¹⁰ The application of the mandatory rules of a third country has been provoking debate since 1966 where the Dutch Court in the *Alnati* case (Hoge Raad, 13 June 1966, RCDIP 1967, 523) stated: “it may be the case that, for a foreign State, the observance of certain of its rules, even outside its own territory, is of such importance that the courts must take account of them, and hence them in preference to the law of another State which may have been chosen by the parties to govern their contract”. See the quotation from Giuliano and Lagarde (*Report on the Convention on the Law Applicable to Contractual Obligations* [1980] OJ C282/1 (Giuliano and Lagarde Report), art 7(1)). See further Marazopoulou “Overriding Mandatory Provisions of Article 9(3) of the Rome I Regulation” 2011 64 *Revue Hellenique de Droit International* 779.

¹¹ This is commonly referred to as the American theory of government interest analysis. This reason is advocated by Chong (“The Public Policy and Mandatory Rules of Third Countries in International Contracts” 2006 2 *Journal of Private International Law* 27–36).

¹² The principle of comity is seen to preserve relations with friendly states, foster international cooperation and encourage reciprocal action by foreign courts. Because of this, the principle of comity as a justification for the application of the mandatory rules of a third country is advocated by Chong (2006 *Journal of Private International Law* 37–38).

by the same precepts as states. It would then also owe a duty of comity to states.

The practice of states in litigation can provide helpful guidance in navigating this issue. The European Union and South Africa follow a very similar line with regard to application of the mandatory rules of a third state: they both favour only the application of the law of mandatory rules of the law of the place of performance, but only in cases where performance is illegal or unlawful in terms of this law (this of course is aside from the law applicable to the contract and the *lex fori*).¹³ The Rome I Regulation sets out these policy considerations in article 9(3), stating:

“[E]ffect may be given to the overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the contract unlawful.”

The policy considerations in terms of article 9 also determine that the nature and purpose, and consequences of the application or non-application (of the law of the place of performance) should be taken into consideration when determining their applicability. Article 9(3) is thus meant to be read in conjunction with article 9(1), which states that mandatory rules should be taken into consideration; this safeguards the state's public interests, such as its political, social or economic organisation.

Another approach can be found in Turkish private international law, which adopts a position very similar to that of the Rome Convention.¹⁴ The Turkish position on overriding mandatory rules can be found in the Turkish Private International Law Act in article 31, which states:

“When the law governing the relationship arising from the contract is being applied, the overriding mandatory rules of third country may be given effect in the case where these rules are closely connected with the contract. Regarding giving effect to and applying or not applying the rules at issue, the purpose nature, content and consequences of these rules shall be taken into consideration.”¹⁵

The Turkish position calls for the application of the closest-connection test. It states that if the country has a sufficiently close connection to the contract, then its mandatory rules may find application. This position is controversial

¹³ In determining in which instances the mandatory rules of another law would be taken into consideration, South African courts are principally guided by English decisions, before the Rome I regulation came into force. In *Henry v Branfield* 1996 (1) SA 244 (D), Levinsohn J stated *obiter* that South African courts would not enforce performance that is illegal under the *lex loci solutionis*. This position is supported by older *dicta* in the form of *Cargo Motors Corporation Ltd v Tofalos Transport Ltd* 1972 (1) SA 186 (W), which also indicates that the courts would only take the *lex loci solutionis* into consideration but at the same time, definitively rules out the *lex loci contractus* (law of the place of contracting). This is a position that is also supported by Professor Forsyth, who states that allowing courts a wide discretion in the application of mandatory rules would diminish legal certainty (Forsyth *Private International Law* 321).

¹⁴ European Economic Community *Convention on the Law Applicable to Contractual Obligations* OJ L 266 (1980) (Rome Convention) art 7.

¹⁵ NAO Boztosun (tr) “The 2007 Turkish Code on Private International Law and International Civil Procedure” in Bonomi and Volken (eds) *Yearbook of Private International Law* vol 9 (2008) 594.

and has been contested. The primary reason for this contention is the issue of legal certainty. The argument goes that by allowing such wide discretion to the court, legal certainty is sacrificed, in that at the time when the parties enter into the contract and select a law to govern their contract, they will not be aware of all the legal systems and all the legal rules that could apply to their agreement.¹⁶ The solution that was adopted (under pressure from the United Kingdom) in the Rome I Regulation (the successor to the Rome Convention) was to allow application of the mandatory rules of a third country only if that country was the place of performance, and then only if performance was unlawful in terms of that country's laws.¹⁷

The above methodologies all start from a similar viewpoint. They look at underlying policy considerations in making their determination. There is a resonance between these approaches and what is known in the United States as the government interest analysis. Article 187(2)(b) of the Restatement Second states that the law chosen by the parties shall not be applied if

“application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially higher interest than the chosen state in the determination of the particular issue and which, under the rule of s 188, would be the state of the applicable law in the absence of a choice of law by the parties.”

The “fundamental policy of a state” referred to underlines the interest of the state that is being protected. In the Rome I Regulation, this is referred to as a political, social or economic interest. Of course, the government interest analysis, as can be seen here, limits the application of a third country's law only to the mandatory rules of the legal system that would have applied in the absence of choice by the parties. This can be equated to the objective proper law, which can further be equated to the closest-connection test. This position and the Turkish position, which applies the closest-connection test, are likely to lead to the same outcome.

The complexity of the matter is further demonstrated by the fact that the Hague Principles, in article 11(5), chose not to address the matter directly, but simply left the arbitral tribunal to make the decision on when it is required or entitled to take into account public policy or overriding mandatory rules that were not chosen by the parties.

A recent arbitration before the International Court of Arbitration of the International Chamber of Commerce (ICC) considered a matter where both parties were Turkish but had chosen German law as the substantive law of

¹⁶ It was precisely for this reason that the United Kingdom, along with several other countries, including Germany and Ireland, entered a reservation against art 7 in the Rome Convention. Their argument was that the reasonable expectations of the parties would never be met if the formulation of the article was left as is.

¹⁷ See the discussion of art 9(3) above. See also art 11(4) of the African Principles on the Law Applicable to International Commercial Contracts, a *via media* approach, where the principles allow for the application of another law in exceptional circumstances where there is a manifestly closer connection (Neels *African Principles on the Law Applicable to International Commercial Contracts* (2023)).

the contract, and Germany as the arbitral seat.¹⁸ The respondent argued that the agreement was invalid because of a mandatory rule of Turkish law, which required that any commercial agreement between Turkish parties was required to be in the Turkish language. As both the substantive law and the *lex arbitri* were German law, it would seem that the tribunal took the view that the arbitration agreement was also tacitly governed by the law of Germany. The validity of the arbitration agreement in this case was thus determined by German arbitral law, which stated that the agreement was valid if it was contained in a document, without any reference to a language requirement.¹⁹ The tribunal also relied on the substantive law to determine the validity of the choice-of-law clause.²⁰ In the view of the present author, this application is correct because the parties had exercised a choice with regard to the applicable law; and the invalidity was contained in the mandatory law of a third country. The tribunal determined further that in considering the application of the mandatory rules of a third country, the enquiry should focus on whether its non-application would render the award unenforceable. As both companies were Turkish companies, in this case, there was a strong likelihood that the arbitral award would be enforced in Turkey. The connecting factor used in this case could then be considered to be the law of the place of potential enforcement.²¹

It must be recalled that the application of the mandatory rules of a third country should be dependent on public-policy considerations. The relevant state must have a fundamental interest in having its law applied in the matter. If there is such an interest, then a determination could be made on whether the place of potential enforcement would recognise and enforce the agreement. In this case, the connecting factor to Turkish law was the domicile (or nationality) of the companies. The provision requiring the language of the contract to be Turkish, however, did not seem to indicate in any material way that the interest being protected was necessary to safeguard the public interests of Turkey. The rule of Turkish law in this case was only a rule of formal validity and therefore should not be interpreted as a mandatory rule in any event.²²

The policy considerations of states whose laws have not been chosen and would not otherwise be applicable are a source of much consternation in arbitration. It could be argued that an arbitral tribunal is not bound to consider the policy of states whose laws have not been chosen; however, the consequence of such a position is that the award could be rendered void when enforcement is sought. Berman's argument, where he determines that the tribunal is only bound to the mandate granted to it by the parties, must be considered. Exceeding this mandate by applying the mandatory rules of a third country may render the arbitration void in terms of both the arbitral *situs*

¹⁸ Van den Berg (ed) "*Seller (Turkey) v. Buyer (Turkey)*", Final Award, ICC Case No. 16168" 2013 38 *Yearbook Commercial Arbitration* 205–227.

¹⁹ Van den Berg 2013 *Yearbook Commercial Arbitration* 213.

²⁰ Van den Berg 2013 *Yearbook Commercial Arbitration* 206.

²¹ See Nygh (*Autonomy in International Contracts* (1999) 232), who seems also to favour this approach.

²² See art 5 of the Hague Principles, which states: "A choice of law is not subject to any requirement as to form unless otherwise agreed by the parties."

as well as the place of enforcement.²³ In other words, considerations of comity are overridden by the mandate granted to the tribunal by the parties. A solution proffered is that the ultimate mandate granted to the tribunal by the parties is to resolve the matter in its entirety.²⁴ It is not in the interest of parties to not apply an otherwise applicable mandatory rule that will be taken into consideration at the place of enforcement, as this would render the award meaningless. Consensus by the arbitral legal order may also provide a solution. If tribunals consider themselves duty-bound to apply the mandatory rules of a third country, consensus could be reached that considers the application of such rules as part of the rules of the arbitral legal order. Lando expresses this in reference to article 7(1) of the Rome Convention, where he states that it is expressive of international solidarity.²⁵ An outlook of this nature imposes an obligation on tribunals to consider the international arbitral legal order of which they form part and on which they depend, and to acknowledge that this order rests on the goodwill of the legal orders of states by which it is surrounded. In reference to the precise connecting factor that may be applicable, Nygh ends his discussion in a pragmatic manner, stating that in the ultimate analysis, it is the law of the place of likely enforcement that counts.²⁶

There is a final consideration that must be taken into account when considering the application of the mandatory rules of the law of the place of enforcement – namely, that not all awards need to be enforced. This question is of interest because it means that the mandatory rules of the place of enforcement are activated only once enforcement is sought, and moreover, they may not have a bearing on the contract before that. This possibility could, in fact, lead to the conclusion that it is not possible for the tribunal to determine beforehand all the laws that may be applicable to the agreement. In such cases, the tribunal may be better served by applying only the laws that are currently applicable to the agreement in its entirety, and not making a decision on the basis of a law that may apply in the future. This conundrum brings the question full circle. The adoption of the international public-policy doctrine that is discussed below may, to a limited degree, mitigate the uncertainty created by the mandatory rules of a third country as they apply in arbitration.

4 THE MANDATORY RULES OF THE SEAT

The mandatory rules of the seat are the next set of rules that must be considered. From a private international law perspective, the question of the legal seat must be considered from the viewpoint of its connection to the

²³ Art V(1)(c), which allows non-recognition in the case where the arbitral tribunal exceeds its mandate.

²⁴ Berman *International Arbitration and Private International Law* 24 (2017) 409. Nygh (*Autonomy in International Contracts* (1999) 232) also refers to this as a pragmatic solution. See also art 6 of the ICC Rules, which states: "[W]hen the court scrutinizes draft awards in accordance with article 34 of the Rules, it considers, to the extent practicable, the requirement of mandatory law at the place of arbitration."

²⁵ Lando "The Lex Mercatoria in International Commercial Arbitration" 1985 34 *International and Comparative Law Quarterly* 747 767.

²⁶ Nygh *Autonomy in International Contracts* 232.

contract. Commentators who favour the territorial approach would consider the mandatory rules of the legal seat as being applicable to the totality of the contract.²⁷ However, the question is slightly more nuanced. If one begins from the viewpoint of considering the seat's connection, it becomes clear that the purpose of the seat is only to host the arbitration.²⁸ The parties select an arbitral seat (where they have applied their minds to the question) on the basis of the arbitral framework that it provides.²⁹ If this approach is followed through, this means that it is, in fact, only the *lex arbitri* that applies to the contract. The parties certainly did not choose the seat because of the substantive law of the country of the seat. The natural conclusion to be reached then is that it is only the mandatory rules of the arbitral law that could apply to the contract, while the substantive mandatory rules of the seat would have no application.³⁰ If the parties specifically chose the substantive law of the agreement, the inference is even clearer.³¹

The application of the UNCITRAL Model Law may place an award rendered by an arbitral tribunal at some risk if the above-stated position were accepted. Article 34(2) states that "the arbitral award may be set aside if the award is in conflict with the public policy of this State". The arbitral law of any state that had adopted the UNCITRAL Model would therefore provide for the award to be set aside by a competent court in the jurisdiction of the seat. The tribunal is ultimately tasked with rendering an award that is enforceable; the failure to take into account the public policy or mandatory rules of the forum (in terms of the model law) may therefore have the effect of rendering the award unenforceable.³² The courts are likely to be directed to the Model Law (where it is applicable) by the private international law rules of the forum. The New York Convention provides the private international law rule in this regard. Article V(1) stipulates that recognition and enforcement of an award *may* be refused if the award has been set aside by the state in which, or under the law of which, the award was rendered.³³ The reference to the word "may" provides the court of enforcement with discretion in this regard. It need not refuse enforcement in these cases, but it may do so. Which circumstances should guide the court in this regard? The private international law rule in this case points to the law of the seat. There is a high likelihood that the law of the seat would be the UNCITRAL Model Law (because of the number of countries that have adopted the model law), and

²⁷ This follows naturally from the territorial thesis. See also Paulsson "Arbitration in Three Dimensions" 2011 60 *International and Comparative Law Quarterly* 293.

²⁸ See Berman (*International Arbitration and Private International Law* 24 215–232), where he considers the regulatory and supervisory role of being a host state.

²⁹ This was explored above.

³⁰ Berman *International Arbitration and Private International Law* 24 397; Nygh *Autonomy in International Contracts* 228. See also *Mitsubishi Motors Corp v Soler Chrysler Plymouth Inc* 473 US 614 (1985) 636: "where the courts state that the international arbitral tribunal owes no prior allegiance to the legal norms of particular States; hence it has no direct obligation to vindicate their statutory dictates".

³¹ Berman *International Arbitration and Private International Law* 24 398.

³² Nygh *Autonomy in International Contracts* 228. See also the General Rule of art 42 of the ICC Rules, which states: "In all matters not expressly provided for in the Rules, the Court and the arbitral tribunal shall act in the spirit of the Rules and shall make every effort to make sure that the award is enforceable at law."

³³ United Nations *Convention on the Recognition and Enforcement of Foreign Arbitral Awards* 330 UNTS 3 (1958) (New York Convention) art V(1)(e).

article 34 would therefore be applicable. The question may, however, arise as to why the public policy of the state hosting the arbitration should find any application if it is only the arbitral law of the country that should apply? In the absence of another link, such as the domicile of one of the parties, or a party being a consumer, there is no connection to the state, and the mandatory rules or public policy of the state should not be an issue under consideration.

The question of the arbitrability of a matter, therefore, becomes important at this stage. The classification of a matter as either part of the substantive law, the law of the arbitration agreement or the arbitral law is important in determining which legal system's mandatory rules are applicable to the arbitration. It will be recalled that Berman refers the matter to the law of the place under which the cause of action arose.³⁴ He argues against conflating arbitrability of a matter with public policy,³⁵ considering it far more desirable that one body of law should govern issues of arbitrability, regardless of the stage of the life cycle of the arbitration – be it at the time of enforcement of the agreement, the time at which an order setting aside the award is pursued, or at the time of enforcement of the award.³⁶ The present author finds it difficult to accept this view for a number of reasons. Berman argues that the arbitrability of a matter cannot be determined by the state of enforcement because the state of enforcement is not likely to be known at the time that the arbitration commences.³⁷ This may well be so, but this is not in itself a reason to exclude the application of the mandatory rules of the state of enforcement. If the matter is approached from the perspective of whether the state has an interest in the matter that is worthy of protection, the natural answer in this case would be yes. The state of enforcement has every right, as a sovereign legal order, to determine that it will not assist an arbitration that, in its view, is abhorrent.

This is demonstrated in the English case of *Soleimany v Soleimany*.³⁸ In this case, the substantive law of the agreement was Jewish law (a non-state law). The dispute involved the smuggling of carpets out of Iran. According to the expert witnesses on Jewish law, this did not invalidate the contract. The English court, however, took the view that public policy would not allow a contract to be upheld where the contract was illegal. The interesting point is that, in this case, the illegality did not arise in terms of the substantive law of the contract or even in terms of the law of the place of enforcement of the award, but rather in the place of performance.³⁹ The English court thus allows application of the mandatory rules of the law of the place of performance. This case demonstrates very simply why the mandatory rules of the substantive law could not be the only mandatory rules applicable to the agreement. The parties could, by resorting to a non-state law, ensure that their entire arbitration was delocalised and that no mandatory rules whatsoever applied to them. The arbitrability of a matter would therefore be

³⁴ Berman *International Arbitration and Private International Law* 24 188.

³⁵ Berman *International Arbitration and Private International Law* 24 187.

³⁶ Berman *International Arbitration and Private International Law* 24 188.

³⁷ Berman *International Arbitration and Private International Law* 24 186.

³⁸ [1999] QB 785.

³⁹ Blackaby, Partasides and Redfern *Redfern and Hunter on International Arbitration* (2016) par 11.106.

dependent on the legal system at the stage of the life cycle of the arbitration, because all legal systems could probably demonstrate an interest in the matter. The place of arbitration affords the arbitral legal order the space and regulatory framework in which to conduct the arbitration; its rules must be respected by the tribunal. The place where an application is made in order for the arbitral award to be set aside is also usually the place of the legal seat of the arbitration.⁴⁰ Both instances, therefore, refer to only one legal system. The only other legal system of potential applicability is the law of the place of enforcement.

5 PUBLIC POLICY

The overlap between public policy and mandatory rules is clear. From the private international law perspective, mandatory rules fulfil a similar function insofar as their effect is to override the otherwise applicable law. Mandatory rules often have a public-policy function at their heart, so the difference between the two types of rules is not always distinct. Public policy would, however, operate more defensively than mandatory rules, as they prevent the application of a law where the law itself, or the consequences of its application, are offensive.⁴¹ The question, as it has been raised throughout this article, is then to consider to which state the public policy is offensive? In litigation, it is an offence against the public policy of the forum that is critical, but this is because the court in such a case has a duty to protect the interests of the state and to ensure that practices that are abhorrent to it are not allowed in the state. An arbitral tribunal that holds hearings on the territory of a certain state cannot be said to hold the same allegiances.⁴² The same arguments that were produced in the case of mandatory rules can be considered in this context. If the parties have chosen a certain state as the arbitral *situs*, their considerations, in making such a choice, are usually only the application of the country's arbitral law. The present author would suggest that only notions of the state's public policy that are applicable as part of its arbitral law should then be considered in the context. One could read article V(2)(b) and articles 34 (2)(b)(ii) and 36 (2)(b)(ii) of the New York Convention and Model Law in this light. Article V(2)(b) stipulates that an award may not be recognised and enforced if it is contrary to the public policy of the state where the award was made. The articles of the Model Law reinforce this by allowing the courts of the forum to set aside an award where the award conflicts with the public policy of the forum state. The provisions could be read in a limited context, not considering the entirety of the state's substantive law as being applicable on public-policy grounds, but only those that are directly related to arbitration. The arbitrability of a matter is likely to fall into this category. There is a safeguard that applies in this context: where the public policy of the national state is so idiosyncratic or hostile to arbitration as to offend the accepted norms of the arbitral legal order, then those policies need not be upheld.⁴³ Even if an award were set

⁴⁰ See art VI, read with art V(1)(e) of the New York Convention.

⁴¹ Berman *International Arbitration and Private International Law* 24 414–415.

⁴² Berman *International Arbitration and Private International Law* 24 416.

⁴³ Berman *International Arbitration and Private International Law* 24 418.

aside at the arbitral seat that harboured these tendencies, the award could still be enforced in an alternate jurisdiction.⁴⁴

Another way in which the arbitral legal order is limited by the formal legal order of states is in the area of arbitrability. The arbitrability of a matter considers whether the arbitration agreement is valid by virtue of it being a matter that could, in fact, be legally determined by way of arbitration.⁴⁵ There is no international consensus on which matters are non-arbitrable.⁴⁶ However, there are some recurring themes, such as criminal claims, patent and trademark claims, competition and securities-law claims, claims involving insolvency, claims involving natural resources, and claims arising out of bribery, corruption and fraud. Article V(2)(a) of the New York Convention states:

“the recognition and execution of an arbitral decision may also be refused if the competent authority of the State in which the recognition and execution is requested finds: (a) that the subject of the dispute cannot be settled by arbitration under the law of that State”.

The New York Convention does then consider, albeit indirectly, the arbitrability of a matter in determining whether an award should be recognised and enforced.⁴⁷ It does not, however, provide for which matters should be considered arbitrable or non-arbitrable, appearing to leave this to the state where enforcement of the award is sought. Berman argues that the New York Convention considers the matter only at the enforcement stage, and not at the stage where the arbitration agreement is invoked.⁴⁸ The parties do not know where the agreement is going to be enforced at the time that the agreement is invoked, which therefore renders the place of enforcement unsuitable as the law governing the arbitrability of a matter.⁴⁹ In his view, the only jurisdiction that has enough of an interest in the matter to warrant governance of the issue is the law under which the cause of action arose.⁵⁰ One presumes that he refers here to the substantive law of the agreement. However, there are other options: the law of the place where the arbitration is held – the *lex arbitri*, the law of the otherwise competent court, the law of the arbitration agreement and the law of potential enforcement.⁵¹ Berman argues that arbitrability and public policy should not be conflated.⁵² They are separate issues in his view.

⁴⁴ *Ibid.*

⁴⁵ Berman *International Arbitration and Private International Law* 24 179.

⁴⁶ Berman *International Arbitration and Private International Law* 24 184.

⁴⁷ The Convention also considers the arbitrability of a matter in art II(1), which stipulates that “[e]ach contracting party shall recognise an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect to a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration”.

⁴⁸ Berman *International Arbitration and Private International Law* 24 183.

⁴⁹ Berman *International Arbitration and Private International Law* 24 185.

⁵⁰ Berman *International Arbitration and Private International Law* 24 188.

⁵¹ Berman *International Arbitration and Private International Law* 24 189.

⁵² *Ibid.*

In a partial award of the ICC in 1996, all three matters were present – mandatory rules, public policy and arbitrability.⁵³ The *lex arbitri* in the case was Swiss law. The defendant resisted the arbitral process on the basis of the Italian Civil Code, which, it submitted, necessitated that the matter come before an Italian court as a matter of labour law.⁵⁴ The sole arbitrator determined that this was, in fact, a matter of arbitrability.⁵⁵ The tribunal considered whether the rule – as mandatory rules of a third country – had any applicability. As Swiss law was the law of the seat, Italian law (as the mandatory rule of a third country) had no application in the view of the tribunal.⁵⁶ The question that still merited an answer, however, was whether the decision not to observe the jurisdiction of the Italian court in terms of the provisions of the Italian Civil Code amounted to a violation of public policy.⁵⁷ In order to make this determination, the arbitrator embarked on a substantive review of the provisions to determine their nature and purpose and in so doing, to determine the nature of the Italian state's interest in the matter.⁵⁸ The analysis led the tribunal to conclude that it was not a violation of Italian public policy to disregard the provisions of the Italian Civil Code. As a concluding remark on this case, it is interesting to note that the tribunal also defined public policy in terms of Swiss law.⁵⁹

The idea behind international public policy is that the enforcement of an award should be denied or set aside only in cases where the public-policy rule adopted to set it aside is one that is held by the international community at large. The basis for such an agreement is limited and can truthfully only be set out in broad terms. Transnational public policy could be defined as “norms that are considered so basic to a just and decent society that they cannot be derogated from either by the parties or the arbitral tribunal, whatever might be the law that the parties chose to govern their dispute”.⁶⁰ The range of such norms is obviously limited and includes issues such as slavery, bribery, piracy and human-rights violations.⁶¹ The application of public policy would seem to indicate that the tribunal still refers to the laws of states for the primary rules of public policy, but applies international public policy as overarching rules that provide a baseline to or upon which arbitrators can refer or depend.⁶² Of course, the cases in which arbitral tribunals would have to look beyond a single state's public policy to uphold

⁵³ Van den Berg (ed) “*Agent v Supplier*, Partial Award, ICC Case No. 8420, 1996” 2000 15 *Yearbook Commercial Arbitration* 328–340.

⁵⁴ The defendant relied on arts 409 and 413 of the Italian Code of Civil Procedure, which reserved exclusive jurisdiction to the Italian courts on matters that were considered to be agency and commercial agency relations of an individual that was of a continuous nature.

⁵⁵ Van den Berg 2000 *Yearbook Commercial Arbitration* 330.

⁵⁶ Van den Berg 2000 *Yearbook Commercial Arbitration* 331–332. See art 176(1) of the Swiss Private International Law Act of 1987 on which the tribunal determined the law applicable to arbitrability, which was Swiss law. The tribunal then proceeded to apply art 177(1), which allowed any dispute that concerned a financial interest to be arbitrable.

⁵⁷ Van den Berg 2000 *Yearbook Commercial Arbitration* 334.

⁵⁸ Van den Berg 2000 *Yearbook Commercial Arbitration* 335–336.

⁵⁹ The tribunal here relied on the meaning of public policy in terms of the law of the *lex arbitri*. See art 190(2)(e) of the Swiss Private International Law Act of 1987 for the definition of public policy relied on by the tribunal.

⁶⁰ Berman *International Arbitration and Private International Law* 24 419.

⁶¹ *Ibid.*

⁶² Berman *International Arbitration and Private International Law* 24 423.

public policy on any of the issues mentioned above would have to be severely limited. It is highly unlikely that the public policy of any state would not override contracts that upheld slavery, piracy or human-rights violations.⁶³

6 CONCLUSION

The article explores the concepts of mandatory rules and public policy as a limitation on party autonomy in the arbitral context. It highlights the differences between their application in international litigation and international arbitration respectively, and considers the different bases for their application. It concludes that the mandatory rules that would often find application in international litigation are not a given in international arbitration. With regard to the application of the mandatory rules of the proper law, the article provides the context in which these mandatory rules could apply, namely, after a consideration of the wording of the choice-of-law clause. As to the application of the mandatory rules of a third country, the article provides the reasoning on which the laws of third countries should be taken into consideration, but concludes that the mandatory rules most likely to find application, in this context, would be the law of the place of enforcement. Application of the mandatory rules of the arbitral seat is also considered. In this context, the article considers the overlap between the arbitrability of an issue and the mandatory rules. The article proposes that, subject to the nature of the mandatory rules, the mandatory rules of the arbitral seat may be taken into consideration. Consideration of their nature revolves predominantly around public-policy grounds. The point is made that the place where the arbitral proceedings are held (the place of enforcement of the agreement) affords the arbitral legal order the space and regulatory framework in which to conduct the arbitration, and its rules should therefore be respected. The place where an application is made in order for the arbitral award to be set aside is also usually the place of the legal seat of the arbitration.⁶⁴ Both instances, therefore, refer to only one legal system. The only other legal system of potential applicability is the law of the place of enforcement.

⁶³ Pryles "Reflections on Transnational Public Policy" 2007 24 *Journal of International Arbitration* 6. He also cautions that the arbitrator would be likely to apply their own notion of what international public policy was where there was uncertainty as to its content. The possibility also exists that parties could vexatiously attempt to rely on international public policy in order to have a contract rendered void. See in general, *Customs and Tax Consultancy LLC v Democratic Republic of Congo* (Final Award), 22 February 2016 *Arbitrator Intelligence Materials*.

⁶⁴ See art VI, read with art V(1)(e) of the New York Convention.