The Effect of the Rome I Regulation upon Parties' Choice of Non-State Law and *"Amiable Composition"* in Arbitration

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Abstract:

The study aims to explore the effect of the Rome I Regulation upon parties' choice of non-state law or resolving the dispute '*amiable composition'* in arbitration. Although it is argued by some commentators that these concepts cannot be applied to arbitration as an effect of the Regulation, nevertheless the study concludes that parties are allowed to choose non-state law to be applied and arbitrators are obliged to follow their choice. Although the Rome I regulation does not have any effect in choice of law rules in arbitration, this does not mean that the arbitration system is completely free from the Rome I Regulation. For example, arbitrators like judges are obliged to apply the mandatory rule of law within Europe.

Key words: the Rome I Regulation, arbitration, non-state law, amiable composition', mandatory rules.

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1- Introduction

It is utmost acceptable that non-state rules be applied in arbitration. The UNICTRAL Model Law [1] gives a plain

1 UNCITRAL Model Law on International Commercial Arbitration 1985 (Model Law).

indicator,[1] whereby the arbitral tribunal will apply the law or "rules of law'' which have been chosen by the parties involved.[2] This freedom of choosing a-national law was construed by the Explanatory Notes of the Model Law.[3] Parties can resort to arbitration and therefore can determine which law will apply.[4] However, there are varying opinions about the situation according to the Rome Convention[5] and Rome I Regulation.[6]

1 Article 28(1) Model Law.

2 Fountoulakis, 'The Parties' Choice of 'Neutral Law' in International Sales Contract ' (2005) 7 European Journal of Law Reform 303, 325.

3 'By referring to the choice of "rules of law" instead of "law", Model Law broadens the range of options available to parties as regards to the designation of the law applicable to the substance of the dispute. For example, parties may agree on rules of law that have been elaborated on by an international forum but have not yet been incorporated into any national legal system. Parties could also directly choose an instrument such as the United Nations Convention on Contracts for the International Sale of Goods as the body of substantive law governing the arbitration, without having to refer to the national law of any State party to that Convention'. The explanatory Notes, p 33. <http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf> accessed 02 July 2011.

4 Friendrich Juenger, 'The UNIDROIT Principles of Commercial Contracts and Inter-American Contract Choice of Law' Contratación international, Comentarios a los Principios sobre los Contratos Comerciales Internationales del Unidriot, Unversidad Nacional Autónoma de México - Unversidad Panamericana (1998) 229, 231.

5 EC Convention on the Law Applicable to Contractual Obligation 1980 (Rome Convention).

6 Regulation (EC) No 593/2008 on the Law Applicable to Contractual Obligation (Rome I).

The Rome I Regulation excludes arbitration agreements from its scope according to Article 1(2)(d). This exclusion gives rise to different interpretations. The first interpretation is that the Rome I Regulation does not apply in arbitration, while the second one is that it excludes arbitration agreements from its scope which means that arbitrators are obliged to apply the regulation in relation to the merits of the dispute(s) at hand.

These interpretations have no effect if parties choose a law of a state or the CISG.[1] This is due to the fact that both are a law of a state and both arbitration Acts and the Rome I Regulation give parties the right to choose a law of a State. The problem is in applying non-state- law or 'amiable composition'. According to some interpretations, by applying the Rome I Regulation in arbitration, parties are deprived of choosing non-state law as the Regulation specifies "the law of a state". However, Recital 13 of the Regulation gives parties the right to choose non-state rules by incorporating them in the contract. As a result, parties are not entitled to empower arbitrators to resolve the dispute amiable composition.[2] The contradicting approaches in this issue give several arguments and counter arguments which will be discussed below.

2. The Exclusion Scope

The exclusion scope in the Rome I Regulation is not free from doubt. It could be argued that the exclusion covers the arbitration clause while the dispute referred to arbitration is

1 United Nations Convention on Contracts for the International Sale of Good (1980) (CISG)

2 Burcu Yuksel, 'The Relevance of the Rome I Regulation to International Commercial Arbitration in the European Union' (2011) 7(1) Journal of Private International Law 149, 170.

included.[1] This was the same attitude in the Rome Convention. The arbitration clause remains in the ambit of the common law and substantive issues operate within the Rome Convention.[2]

The Giuliano and Lagards Report highlight the exclusion by stating 'Where the arbitration clause forms an integral part of a contract, the exclusion relates only to the clause itself and not to the contract as a whole'.[3] It could be inferred that the report gives an indirect indicator, separating the arbitration clause from the matrix contract. According to this understanding, the Rome I Regulation will apply in order to determine the governing law to the merits of the dispute.[4] This current article gives several arguments for this understanding to the Regulation scope as follows.

2.1 The conclusion that the Rome I Regulation applies in arbitration could be strengthened by a comparison between the Brussels I Regulation[5] and the Rome I Regulation. While the former excludes "arbitration" from its scope according to Article 1(2)(d).[6] Although Brussels I Regulation deals with enforcement and recognition of judgment, Rome I Regulation deals with the applicable rules

1 ibid 154.

2 A.E.Anton & P.R.Beaumont, *Private International Law, A treatise from the standpoint of Scots law* (2nd edn, W.Green 1990) 360.

3 Giuliano and Lagarde Report on the Convention on the law applicable to contractual obligation by Mario Giuliano and Paul Lagarde, Official Journal C 282, 31/10/1980, P 10 .

4 D. Lasok & P. A. Stone, *Conflict of Law in the European Community* (Professional Books limited 1987) 353.

5 Council Regulation [EC] No 44/2001 on jurisdiction and recognition and enforcement of judgment in civil and commercial matters.

6 Yuksel (n 9) p. 153.

in general. This does not mean depriving parties from choosing non-state rules and all aspects of arbitration are included. However, there are some rules included which act as mandatory rules.

2.2 Rome I **Recitals**:

Recital 12 of the Rome I regulation provides*:* 'an agreement between parties to confer on one or more than courts or tribunal of a member state exclusive jurisdiction to determine disputes under the contract should be one of the factors to be taken into account in determining whether a choice of law has been clearly demonstrated'.

The phrase "choice of tribunal" was repeated in Recital 15, similar to the choice of court in order to determine the applicable law to the dispute.[1] It states that '.... This rule should apply whether or not the choice of law was accompanied by a choice of court or tribunal'. Nevertheless, relying on the above Recitals is an issue not free from doubt, as several Recitals in the Rome I Regulation give indicators that it applies only in litigation and not arbitration. For example, Recital 6 states that**:** 'the proper functioning of the internal market creates a need, in order to improve the predictability of litigation, certainty as to the law applicable and the free movement of judgments, for the conflict-of-law rules in the Member States to designate the same national law irrespective of the country of the court in which an action is brought'. The phrase "court" was repeated in Recitals 8, 16 and 37.

Moreover, the Recitals which state "tribunal" do not give a conclusive indicator that the application of non-state law is the same before arbitration and litigation. For example,

[1] yuksel (n 9) 166.

Recital 15 refers to another issue. It mentions mandatory rules, the application of which is the same in both arbitration and litigation.

3. The Relation between Arbitration Acts and the Regulation within Europe

The vital question here is whether the Regulation supersedes the arbitration Acts in Europe. Some writers[1] argue that the arbitration acts are superseded by the Rome Regulation. The Regulation must be directly applicable in UK and Scotland. This means that provision 46(1)(b) of the Arbitration Act 1996 in England and provision 47 of the Arbitration Act 2010 in Scotland is halted. The difference between regulation and convention is that the former does not need any ratification. The legal nature varies in both instruments.

This leads to the conclusion that the Regulation, unlike the convention, supersedes the national laws, has direct applicability and is binding in all Member States. The arbitrators are bound by regulation and on the event of conflict between the Rules in the Regulation and the Rules in the national laws, the former rules should prevail. Even the Arbitration Act gives the right to parties to choose non-state rules, although this choice will have no effect according to the Regulation.[2]

Nevertheless, it is widely accepted that, unlike judges, arbitrators have no national rules.[3] The seat of international commercial arbitration is usually chosen albeit that it has no connection with

1 ibid 172.
2 Yuksel (n 9) 166.
3 Katharina Boele-Woelki, 'Principles and Private International Law' (1996) 1 Unif. L. Rev 652, 663.

the dispute and the conflict of laws rules of the seat are not necessarily applied by arbitrators.(1)

Most writers(2) whilst discussing the law governing the merits of the dispute in arbitration mention the National Arbitration Act and make reference to Article 46(1)(b) in the Arbitration Act (1996) which allows parties to choose a non-state law according to the term 'other considerations' without any reference to the Rome Convention.(3) Hence, there is no doubt that arbitrators can choose non-state law,(4) or resolve the dispute **'***amiable composition'*.

The Rome Regulation does not extend to arbitration if parties choose non-state law in the ambit of s.46 of the Arbitration Act.(5) Arbitrators are not bound by the Rome I. Unlike judges, the arbitral tribunal is not obliged to apply the Regulation as it is not the "organ of any contracting state".(6) It could be concluded that if the arbitration took place in England, parties would be able to

1 Nigel Blackaby and Constantine Partasides, with Alan Redfern and Martin Hunter*, Redfern and Hunter on International Arbitration* (OUP 2009) 234.

2 C M V Clarkson & Jonathon Hill, *Jaffey on the Conflict of Laws* (2nd edn, Butterworths 2002) 297-298; Carole Murray and others, *Schmitthoff's Export Trade, The Law and Practice of International Trade* (11th edn, Sweet & Maxwell 2007) 550**.** Sir Lawrence Collins**,** *Dicey, Morris & Collins on the Conflict of Laws* (14th edn, Sweet & Maxwell 2008) s.16-019**;** Ewan McKendrick, *Good on Commercial Law* (4th edn, Lexis Nexis 2009) 1320; Blackaby & Partasides (n 20) 227**.**

3 Now Rome I Regulation.

4 Fraser Davidson, *Arbitration* (W.Green, Edinburgh 2000) 302.

5 Richard Plender and Michael Wilderspin, *The European Private International Law of Obligation* (Thomson Reuters 2009) 139**.**

6 Michael Bogdan, *Concise Introduction to EU Private International Law* (Europa Law Publishing 2006) s. 7.1.

choose non-state law to be applied, according to s.46, and the Rome I would not applicable.(1)

4. Judicial Decisions

It was held in *Chalbury v Foils*(2) that in the absence of choosing the *lex causae* by parties in a dispute referred to arbitration, the court has to determine the applicable law in order to exercise its jurisdiction under section 2(4) of the Arbitration Act. The contract includes a clause that the dispute will be referred to as "arbitration as per prevailing laws of European Union in the Europe".(3) The court applied the Rome I Regulation in order to determine the applicable law.(4)

Nevertheless, this case does not give a clear indicator for the application of the Rome I Regulation in arbitration. In this case, the court used the Rome I Regulation in order to decide the seat of arbitration according to the Arbitration Act section 2(4) which demanded a connection with England or Northern Ireland. The court found the connection through a provision designating the applicable law in the contract "arbitration as per prevailing laws of European Union in the Europe". However, this does not give a clear example, because the court applied Article 4 of the Rome I Regulation, which designates the applicable law in the absence of choice by given parties.

A clear example is that of the *Josef Syska v Vivendi Universal*[5] case which expressly stated the non applicability of the Rome Convention to arbitration. It was held that 'the

1 Stone P, *EU Private International Law, Harmonization of Laws* (Elgar European Law 2006) 275.
2 [2010] EWHC 2050 (TCC)
3 Ibid para [25].
4 Ibid para [26].
5 [2008] EWHC 2155 (Comm)

Rome Convention does not apply to arbitration'.[1] According to the Arbitration Act 1996, parties can choose a-national rules.[2] In *Musawi v RE International* (3) *for instance,* the court held that parties can choose any rules of law according to the Arbitration Act 1996.

Mr Justice David Richards stated in relation to this point that:

"section 46(1)(b): allows the parties the freedom to apply a set of rules or principles which do not in themselves constitute a legal system. Such a choice may thus include a non-national set of legal principles (such as the 1994 UNIDROIT Principles of International Commercial Contracts) or, more broadly, general principles of commercial law or the *lex mercatoria*."(4)

The supreme court of Canada held that[5] 'Arbitration is part of no state's judicial system... the arbitrator has no allegiance or connection to any single country.... in short, arbitration is a creature that owes its existence to the will of the parties alone'.

However, some writers([6]) give examples of the ECJ decisions in several cases such as *Broekeulen v Huisarts.*(7) Nevertheless, these cases do not give a certain conclusion in applying the Rome I Regulation, as these decisions concern the mandatory rules of the EU which are not conflicting.

1 ibid para [99].
2 C. M. Clarkson and Jonathan Hill, *The Conflict of Laws* (3rd edn, Oxford 2006) 256.
3 [2007] EWHC 2981 (Ch).
4 Ibid para 20.
5 *Dell Computer Crop V Union* 2007 SCC 34, (2007) 284 D.L.R. (4th) 577, at [51]. As cited by Collins (n 21) s.16-032.
6 Yuksel (n 9) 160-63
7 Case C-102/81 [1981] ECR 2311.

5. Advantages of Arbitration Over Litigation

Unlike arbitration, it is widely accepted that parties exercise partial autonomy in litigation(1). However, it is argued that if the Rome I Regulation is not bound in arbitration and parties exceed the partial autonomy in litigation, this will put arbitration agreements in a better position than one of a choice of courts.(2)

Nevertheless, party autonomy is one of the fundamental characteristics of international arbitration. Parties choose arbitration as a method to resolve their disputes in order to exercise the freedom to choose the law or rules of law they consider suitable for them.(3) Arbitration is a flexible dispute resolution method which works separately to the "nation state".(4) This flexibility reflects the needs of international contracts which need to be governed by appropriate rules of law, such as the UNIDROIT Principles.[5]

6. Concluding Remarks

It is widely accepted that the EU rules which have a mandatory nature must be applied in both arbitration and litigation. As a result of the *Ingmar GB Ltd v Eaton Leonard* case,[6] ignoring these rules may result in a refusal of the

1 Megan Richardson and Richard Garnett, 'Choice of Law and Forum in International Commercial Contracts: Trends in Common Law Jurisdictions (A Non-European Perspective)' 2. <http://www.ialsnet.org/meetings/business/RichardsonMegan-Australia.pdf> accessed 01 July 2011.

2 Yuksel (n 9) 173.

3 Chukwumerije Okezie , *Choice of Law in International Commercial Arbitration* (Greenwood Press 1994) 108.

4 Richardson & Garnett (n 38) 3.

5 ibid 3.

6 Case C-381/98 [2000] ECR 1-9305.

enforcement of the award or annulment. Generally however, ignoring the right to choose the law to be applied does not have this effect with some exceptions, such as in certain England and Scotland Acts which permit a judicial review in the case of a legal error.[1]

In the meantime, the NY Convention[2] requires that courts of the contracting Member State recognize arbitration awards without a judicial review of the arbitrators' award and which choice of law rules they applied. This means that if arbitrators apply non-state rules, the award could be recognised by another Member State.[3]

From the discussion above, it can be accepted that the Rome I Regulation does not permit applying non-state law in arbitration within Europe. This may indeed result in Europe losing its attraction as a seat of arbitration, from the point of view of arbitration parties. This logic means if the arbitration takes place in a Member State, arbitrators are not allowed to apply non-state law. What makes the matter even more complicated is the fact that in applying Rome I Regulation regarding the inability of arbitrators to apply non-state law in Europe does not only stop in Europe loss of being attractive place of arbitration but also the enforceability of arbitration awards that took place outside the Rome I Regulation member states relaying on non-state law. This is due to the fact that most European States' arbitration Acts do not allow an appeal against the arbitrators' award in a point of law. It is only if the

1 Yuksel (n 9) 174.

2 New York Convention on the recognition and enforcement of foreign arbitration awards 1958 (NY Convention).

3 Symeon Symeonides, 'Contracts Subject to Non-State Norms', (2006) 54 American Journal of Comparative Law 209, 212.

arbitration takes place in England or Scotland, the arbitrators' award could be annulled if they apply non-state rules. This means that applying these rules will differ from one seat of arbitration to another. Therefore, the result of applying them will depend on the seat of arbitration. This logic also works against the unification of the legal system within Europe.

Parties may hence be tempted to choose the seat of arbitration outside England or Scotland and in any place in the world either in Europe or outside Europe if the state of arbitration seat is a Member State of NY, as arbitrators can apply non-state law and the arbitral award will be enforced in any other Contracting State.

The weakness of arguments proposed by opponents of non-state rules in arbitration becomes apparent when they confess that if arbitrators apply non-state law this will not generally lead to a refusal of the arbitral awards. This contradicts the logic that every rule of law must have an effect. Hence, it is not logical to say that the law does not permit arbitrators to apply non-state law but if they do so it will not have an effect.

In conclusion, it is widely believed that parties are allowed to choose non-state law to be applied and arbitrators are obliged to follow their choice. The Rome I Regulation does not have any effect in choice of law rules in arbitration. However, this does not mean that the arbitration system is completely free from the Rome I Regulation, since arbitrators, like judges, are obliged to apply the mandatory rule of law within Europe.

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