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THE GOVERNING LAW: FACT OR LAW? – A TRANSNATIONAL RULE ON ESTABLISHING ITS CONTENT

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I. Introduction

I remember a deliberation many years ago. One of my co-arbitrators, a Canadian, suggested dismissing a claim because – he said – “they have not proven the law”. I was young and inexperienced, and surprised: “But they do not have to prove the law”, I replied. And that is when I realized that we were working on very different assumptions.

The topic of this paper is the status of the substantive law governing the dispute before the arbitrators. Is it a fact to be proven by the parties or is it law to be investigated by the arbitrators?

To avoid any misunderstanding, the topic is not *which* substantive law applies. We assume that this choice has already been made by the parties or the arbitrators. Therefore, we will focus on how to establish the content of the chosen law.¹

To answer this question, I will address three issues:

- First, the state of the law in national courts (1. below);
- Second, the law and practice in arbitration (2. below);
- Third, the emergence of a transnational rule (3. below).

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¹ On the topic, see this author's other publications and the citations they contain: *Iura novit arbiter* – Est-ce bien raisonnable?, in Anne Héritier-Lachat and Laurent Hirsch (eds), *De lege ferenda – Réflexions sur le droit désirable en l'honneur du Professeur Alain Hirsch*, Editions Slatkine Genève, 2004, pp. 71-78; and *The Arbitrator and the Law: Does he/she know it? Apply it? How? And a few more questions*, ITA Newsletter, Vol.18 Nr 3, Summer 2004; also published in *Arbitration International*, 2005, pp. 631-638, and reprinted in this Special Series; see also JULIAN D. M. LEW, *Proof of Applicable Law in International Commercial Arbitration*, in *Festschrift für Otto Sandrock zum 70. Geburtstag*, Klaus Peter Berger, Werner F. Ebke, Siegfried Elsing, Bernhard Großfeld, Gunther Kühne (eds), Heidelberg, 2000, pp. 581-601.

II. National Courts

Let me start by dealing with the practice in national courts. Like my Canadian co-arbitrator, many arbitration practitioners approach the status of the law governing the merits in arbitration by referring to the rules applicable in their home courts. With all due respect, such an approach makes little sense. The situation in national courts and the one in international arbitration are very different. National courts have a *lex fori* and any other law is foreign. Arbitral tribunals have no *lex fori* and, hence, the very concept of foreign law is inappropriate.

Whatever the merits of equating national courts and international arbitration, because the equation is often made, we cannot dispense with looking at the application of foreign law in national courts. It varies significantly. There are two main approaches. Some jurisdictions regard foreign law as a fact that must be proven by the parties and others as law on which the court may *ex officio* conduct its own research.

English law is representative of the first approach². The reason for such an approach is primarily a practical one. As an English court stated in the eighteenth century already, "*the way of knowing foreign laws is by admitting them as facts*"³. In other words, this approach facilitates the courts' access to the content of a law with which it is not familiar.

By contrast, the **Swiss or German legal systems**⁴ treat foreign law as law; the court can or must research foreign law *ex officio*. In Switzerland, this rule is embodied in Article 16 PIL Act:

- 1 "*The contents of the foreign law shall be established by the authority on its own motion. For this purpose, the cooperation of the parties may be requested. In matters involving an economic interest, the task of establishing foreign law may be assigned to the parties.*"
- 2 *Swiss law applies if the contents of the foreign law cannot be established."*

² Admittedly, this may be viewed as an oversimplification. Indeed, in English courts, foreign law is a fact of a very special nature; see RICHARD FENTIMAN, *Foreign Law in English Courts – Pleading, Proof and Choice of Law*, Oxford University Press, Oxford 1998.

³ *Mostyn v. Fabrigas* [1775], quoted by Fentiman fn.2.

⁴ On German law, see JAN KROPHOLLER, *Internationales Privatrecht*, 5th edition, Tübingen, 2004, pp. 625-630. For a comparison of the major European systems on this topic, see TREVOR C. HARTLEY, *Pleading and Proof of Foreign Law: The Major European Systems Compared*, in *International and Comparative Law Quarterly* (1996), vol. 45, part 2, pp. 271-292.

The first sentence sets the rule: the court must establish the content of foreign law *ex officio*, which is the consequence of regarding foreign law as law. The following sentences introduce an exception by permitting the court to require the parties' cooperation or entirely delegate to them the task of establishing what the foreign law is. Finally, Article 16(2) sets forth a default rule in the event that the content of the foreign law cannot be established. In such a case, the court is allowed to resort to Swiss law.

US federal law provides for a similar solution, though with more flexibility, in Rule 44.1 of the Federal Rules of Civil Procedure:

"A party who intends to raise an issue concerning the law of a foreign country shall give notice by pleadings or other reasonable written notice. The court, 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. The court's determination shall be treated as a ruling on a question of law."

In other words, foreign law is law and the court has broad authority to conduct its own research, but no duty to do so.⁵

III. International Arbitration

Having reviewed the practice of national courts, let us now examine the second issue, the law and practice in arbitration. National arbitration laws provide very little guidance. There is, however, one interesting rule in the English Arbitration Act 1996, which departs from the strict view that foreign law is a fact. Section 34(1)(g) of the Act provides that the procedural powers of the arbitral tribunal include determining:

"(g) whether and to what extent the tribunal should itself take the initiative in ascertaining the facts and the law;"

The tribunal's power is subject to party autonomy, i.e. an agreement between the parties would prevail over the arbitrators' determination. Unlike the English Act, Chapter 12 of the Swiss PILAct is silent on this issue, treating the status of the governing law as a matter of procedure. As such, it falls within party autonomy or, if the parties do not make use of their autonomy, within the powers of the arbitrators under Article 182 PILAct. The consequence is

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For an analysis of Article 44.1 Federal Rules of Civil Procedure and its application by U.S. courts, see LOUISE E. TEITZ, *From the Courthouse in Tobago to the Internet: The Increasing Need to Prove Foreign Law in U.S. Courts*, in *Journal of Maritime Law and Commerce*, Vol. 34, No.1, January 2003, pp. 97-118.

that the arbitrators are free to apply whatever method they choose to determine the content of the applicable law. Are there limits to this freedom? To answer this question, one must look to the grounds for annulment of the award. The answer found in cases dealing with annulment of awards is "*iura novit arbiter*". Or in the terms of the Federal Court:

*"Le principe iura novit curia, qui est applicable à la procédure arbitrale, impose aux arbitres d'appliquer le droit d'office."*⁶

This principle has two main effects. First, the award is not *ultra petita* if it is based on legal grounds other than those on which the claimant relied. Second, there is no violation of the right or opportunity to be heard if the tribunal does not consult the parties about the application of the law.

There is an exception to this second effect, however, whenever the arbitrator bases his or her decision on a wholly unexpected legal rule which was not addressed in the proceedings, and which none of the parties could have anticipated to be relevant to the outcome:⁷

"L'arbitre s'apprête à fonder sa décision sur une norme ou un principe juridique non évoqué dans la procédure antérieure et dont aucune des parties en présence ne s'est prévaluée et ne pouvait supputer la pertinence in casu."

What is unexpected is a question of judgment, or in the words of Federal Court: "*Ce qui est imprévisible est une question d'appréciation*"⁸. When assessing the unexpected nature of the rule applied by the arbitral tribunal, the Federal Court exercises restraint, i.e. it does not easily accept that an award is based on an unexpected legal reasoning. It does so to take into account the involvement of lawyers of different legal backgrounds in international arbitration:

⁶ ATF 19.12.2001, 4P.114/2001, cons. 3.a, not reported. On *iura novit curia*, see in particular FRANZ KELLERHALS / BERNHARD BERGER, *iura novit arbiter*, in Norm und Wirkung : Beiträge zum Privat- und Wirtschaftsrecht aus heutiger und historischer Perspektive : Festschrift für Wolfgang Wiegand zum 65. Geburtstag, Eugen Bucher / Claus Canaris / Heinrich Honsell / Thomas Koller (eds), Bern 2005, p. 387, at p. 393; FRANÇOIS PERRET, Les conclusions et leur cause juridique au regard de la règle *ne eat iudex ultra petita partium*, in Etudes de droit international en l'honneur de Pierre Lalive, Christian Dominicé, Robert Patry, Claude Reymond (eds), Basle 1993, p. 595; WOLFGANG WIEGAND, *iura novit curia* vs. *ne ultra petita* - Die Anfechtbarkeit von Schiedsgerichtsurteilen im Lichte der jüngsten Rechtsprechung des Bundesgerichts, in Rechtsetzung und Rechtsdurchsetzung, Zivil- und schiedsverfahrensrechtliche Aspekte, Festschrift für Franz Kellerhals zum 65. Geburtstag, Monique Jametti Greiner, Bernhard Berger, Andreas Güngerich (eds), Bern 2005, p. 127; FRANÇOIS PERRET, Quelques considérations sur le droit d'être entendu au regard de l'adage "*iura novit curia*", in Revue suisse de procédure civile 2005/2, p. 223.

⁷ ATF 130 III 35; see also ATF 18.10.04, 4P.104/2004, cons. 5.4, in ASA Bulletin 2005/1 p.164, at p. 170. WOLFGANG WIEGAND, quoted above at fn.6, pp. 139 ff. with whom FRANÇOIS PERRET, quoted above at fn. 6, Quelques considérations, p. 228, convincingly show that rather than unpredictability, the relevant test should be whether the arbitrator's determination of the law deprives the party of the opportunity of relying on defenses on the merits which would not have arisen under a different substantive rule.

⁸ ATF 130 III 35, cons. 5.

"Il convient de se montrer plutôt restrictif dans le domaine de l'arbitrage international, pour tenir compte de ses particularités ([...]; coopération d'arbitres de traditions juridiques différentes)".⁹

One may debate whether the presence of participants from different legal traditions should not trigger precisely the opposite consequence, i.e., whether the arbitral tribunal should consult with the parties more often, not less, before adopting a specific legal solution.¹⁰

Be this as it may, in looking at possible limits to the arbitrators' freedom, another question that arises is whether the method of establishing the content of the substantive law could justify an annulment for violation of public policy on the ground of Article 190 (2)(e). The Federal Court addressed this question in a decision issued in April 2005.¹¹ The (Swiss) sole arbitrator had requested that the parties prove the differences between the applicable Croatian statute on bills of exchange and Swiss law. He had proceeded in such a manner because both legislations followed the uniform law on bills of exchange. Before the Federal Court, the applicant alleged that the arbitrator had breached the principle *iura novit curia*, which amounted to a violation of *ordre public*. Here one needs to recall that the Federal Court had held earlier that *iura novit curia* imposes on the arbitrators a duty to apply the law *ex officio*.¹² No, held the Federal Court, there is no violation of *ordre public*. Indeed, pursuant to Article 16(1) PILAct, a Swiss judicial court may impose the establishment of the content of foreign law on the parties. This was exactly what the arbitrator had done and, hence, there could be no issue of a violation of *ordre public*.

Now back to our question: are there limits to the arbitrators' power to determine the method of establishing the governing law? Except for limits arising out of a possible agreement of the parties and the requirement that the arbitral tribunal must consult with the parties on the application of an unexpected legal rule, there appear to be none.

Bearing this in mind, let us now look at arbitration practice. Arbitration rules are of little or no assistance. In day-to-day arbitration, is a uniform practice emerging? It may be premature to

⁹ Loc. cit.

¹⁰ One could also ask why the Federal Court makes such a distinction when on numerous occasions it has held that the opportunity to be heard provided in Art. 183(2) PILAct does not differ from the one provided in Art. 4(a) and 29(a)(2) of the Swiss Constitution (FRANÇOIS PERRET, quoted above in fn. 7, *Quelques considerations*, p.227).

¹¹ ATF 27.04.05, 4P.242/2004, cons. 7.3, in Bull. ASA 2005/4 p. 719, at pp. 723-724.

¹² ATF 19.12.2001, quoted above in footnote 6.

affirm so in general terms. I would, however, venture to say that, at least when the arbitrator is unfamiliar with the applicable law, the general understanding is that the parties will put forth the law. Doing so, do they believe that the arbitrator is bound by their submissions? Does the arbitrator feel bound?

IV. A Transnational Rule

These questions lead us to the third and last issue in this presentation, which is a proposal for a transnational rule. What should it be? Drawing from the earlier discussion, three points can be made:

- First, a hard and fast *iura novit curia* rule would be inappropriate in international arbitration. This is due to the transnational legal environment involving participants from different legal cultures, and to the possible difficulties of accessing the applicable law, be it for reasons of language, availability, or reliability of the pertinent sources.
- Second, a pure "law is fact" approach would not be appropriate either. Depending on who the arbitrators are, proving the law may be a futile exercise. For instance, counsel would be ill-advised to submit to a Swiss contract law professor an opinion on contract interpretation under Swiss law.
- Third, any appropriate transnational solution must therefore lie between the two extremes, for instance along the lines of Rule 44.1 of the Federal Rules of Civil Procedure. Specifically, such a transnational rule could read as follows:

"The parties shall establish the content of the law applicable to the merits. The arbitral tribunal shall have the power, but not the obligation, to conduct its own research to establish such content. If it makes use of such power, the tribunal shall give the parties an opportunity to comment on the results of the tribunal's research."

"If the content of the applicable law is not established with respect to a specific issue, the arbitral tribunal is empowered to apply to such issue any rule of law it deems appropriate."

This transnational rule calls for three comments:

- The rule is a merger of different civil procedure traditions. As such it is meant to apply in a transcultural environment. It may nevertheless have to be further adapted to the specific cultures involved and to the needs of the specific case.

- The scope of application of the fallback rule, which provides that the tribunal may apply the rule it deems appropriate when the content of the applicable law cannot be established, is relatively limited. It will only come to bear if the applicable legal system provides no method for filling gaps or if the content and outcome of this method cannot be established.
- To avoid that the tribunal and the parties "work on different assumptions", to come back to my Canadian co-arbitrator mentioned at the outset, the status of the applicable law and a rule such as the one just proposed should be discussed and preferably agreed upon at the initial procedural hearing.