Arbitration in Switzerland

The Practitioner's Guide

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Article 21: Applicable Rules of Law

(1) The parties shall be free to agree upon the rules of law to be applied by the arbitral tribunal to the merits of the dispute. In the absence of any such agreement, the arbitral tribunal shall apply the rules of law which it determines to be appropriate.

(2) The arbitral tribunal shall take account of the provisions of the contract, if any, between the parties and of any relevant trade usages.

(3) The arbitral tribunal shall assume the powers of an *amiable compositeur* or decide *ex aequo et bono* only if the parties have agreed to give it such powers.

I. Purpose of the Provision

1 The purpose of the article is to provide a basis for the determination of the law applicable to the substantive dispute.[1]

2 Article 21 corresponds to Art. 17 Rules 1998. This provision has basically remained unchanged save minor changes to the wording in para. 2. These changes, however, have not affected the substance of the article but rather clarified its purpose.

3 Paragraph 2 of Art. 21 of the 1998 Rules read as follows: "In all cases the Arbitral Tribunal shall take account of the provisions of the contract and the relevant trade usages".

4 The term "rule of law" replaced the simple term "law" to increase the breadth of possibilities.[2] As in the 1998 Rules, the arbitrators are no longer obliged to apply conflicts of laws rules to determine the applicable law. Art. 13(3) of the 1975 Rules only permitted the arbitrators to apply conflict of law rules to reach the applicable law for the dispute.[3]

5 The concept of *amiable compositeur* has been included in the ICC Rules since their inception.[4] The term *ex aequo et bono* has only been added recently.[5]

II. Derogation from the Provision

6 This provision allows the parties great freedom. Not only may they choose the rules of law applicable to the dispute, they may also opt in to allow arbitrators to decide in equity.

7 In one opinion, para. 2 of the 1998 Rules denotes a command to the arbitrators, to apply trade customs and the parties' contractual provisions in any event. This command appears to curtail the parties' right to exclude contractual provisions or trade customs from the repertoire of the arbitrators. The parties can certainly not prevent the application of contractual provisions and trade customs simply by permitting a decision in equity. Even a decision in equity must take customs and provisions of the contract into account. Should the parties wish to exclude trade usages or provisions of the contract from the dispute, they would have to do so explicitly. In practice, however, this will rarely be the case. The same argument holds true under the 2012 version of para. 2.

8 Mandatory rules of law may not be opted out of by the choice of the parties.[6] Public policy, the validity of the arbitration agreement and the issue of arbitrability must be considered under the law of a likely

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1 Fry/Greenberg/Mazza, para. 3-744.
2 Bond/Paralika/Secomb, p. 349.
3 Poudret/Besson, para. 685.
4 Bond/Paralika/Secomb, p. 350.
5 Poudret/Besson, para. 711.
6 Bond/Paralika/Secomb, p. 350; Bühler/Jarvin, *2009*, para. 15.665; Fry/Greenberg/Mazza, paras. 3-744 to 3-776; Reiner/Jahnel, para. 4 at Art. 17; Poudret/Besson, para.706.

enforcement country[7] as well as the law of the seat[8] to ensure that the award will stand.[9] Arbitrators should make all reasonable efforts to ensure an enforceable award.[10]

III. Content of the Provision

A. Scope of the Provision

Article 21 applies to the substantive law, rather than the procedural law, which is contained in Art. 19. Art. 21 includes the law applicable to the validity of the contract.[11] **9**

The provision covers the basis on which decisions of the arbitral tribunal may be rendered. It does not address how the content of the law ought to be proven or whether it can be assumed that the arbitrators know. A recently published report of the International Law Association's International Commercial Arbitration Committee addressed the two topics of applicable law and its content.[12] **10**

B. Paragraph 1

Paragraph 1 gives the parties the freedom to choose the rules of law to be applied to the merits of the case.[13] In the absence of a choice by the parties this paragraph entitles the arbitrator(s) to make an appropriate choice in sentence two. **11**

It is notable that, as it was said before, para. 1 is limited to the choice of the rules of law applicable to the merits, rather than a choice of the procedural law, which is contained in Art. 19. In addition the parties must be mindful in how they formulate their choice, otherwise it may only apply to the contractual dispute, but not other aspects, such as tortuous claims.[14] How far the choice of law of the parties reaches is determined by the tribunal.[15] **12**

The term "rules of law" used in Art. 21 is, as it was mentioned before, broader than the term "law" alone[16] and has been used in a number of other institutional rules. It has been defined nowhere.[17] It has been interpreted to include not only national laws and international instruments, but also *lex mercatoria* and general principles of law.[18] It has also been suggested that "rule of law" encompasses recognized principles and model laws (e.g., Unidroit Principles, Principles of European Contract law) as well as rules and standards of private organizations such as the International Olympic Committee or FIFA.[19] Even a piecemeal application of national law is permissible.[20] **13**

In most cases the parties have chosen the applicable rules of law.[21] When they have not done so the arbitrators are free to apply either conflict of laws rules to arrive at the appropriate substantive law or **14**

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7 Bühler/Webster, paras. 17-52 – 17-53.

8 Bühler/Webster, para. 17-10.

9 Bühler/Jarvin, *2009*, paras. 15.666 – 15.668; Poudret/Besson, para.705.

10 Bühler/Webster, para. 17-59; for a closer discussion, see the commentary on Art. 35.

11 Bühler/Webster, para. 17-1; Fry/Greenberg/Mazza, para. 3-745.

12 De Ly/Friedman/Radicati di Brozolo, *ArbInt. 2010*, pp. 193-220.

13 Lachmann, para. 3156; Bühler/Webster, para. 17-3.

14 Bond/Paralika/Secomb, p. 350; Bühler/Webster, paras. 17-31 to 17-32, with further references.

15 Reiner/Jahnel, para. 3 at Art. 17.

16 Bühler/Jarvin, *2009*, para.15.654; Fry/Greenberg/Mazza, paras. 3-747 and 3-760.

17 Bühler/Jarvin, *2009*, para.15.660.

18 Bond/Paralika/Secomb, p. 349; Bühler/Jarvin, *2009*, para. 15.660; Reiner/Jahnel, para.2 at Art. 17; for statistics covering which laws are chosen most often in different parts oft he world, see Fry/Greenberg/Mazza, para. 3-763.

19 Müller-Chen, *SpuRT 2007*, pp. 160-161.

20 Bühler/Jarvin, *2009,* para. 15.660; Fry/Greenberg/Mazza, para. 3-761; Reiner/Jahnel, para. 7 at Art. 17.

21 Bond/Paralika/Secomb, p. 349; Bühler/Jarvin, *2009*, para. 15.656; Bühler/Webster, paras. 17-10 to 17-11; Poudret/Besson, para. 676; De Ly/Friedman/Radicati di Brozolo, p. 195; Fry/Greenberg/Mazza, para. 3-750: in the year 2011, the parties chose the applicable law in 84% of the registered cases.

determine the law applicable to the merits directly.[22] This decision will usually take the form of a partial award or will be determined in the terms of reference.[23]

15 The decision of the arbitrators must be justifiable,[24] especially in light of annulment or obstacles to enforcement.[25] The choice of the arbitrators may not come as a surprise to the parties.[26] In Switzerland, the arbitrators are free to choose,[27] but are to choose the law with the closest connection to the case.[28] (Art. 187(1) PILS) This approach based on the closest connection has only minimal differences to the direct method.[29]

C. Paragraph 2

16 This paragraph may appear surprising only by the fact that it is mentioned explicitly.[30] In the 1998 version, it instructs the arbitral tribunal to take account of the provisions of the contract and the relevant trade usages in all cases. The current version clarifies that the arbitral tribunal shall apply the provisions of the contract and trade usages only if they actually exist, regardless of the applicable law. The change in the wording was made in recognition of the growth in arbitration based on non-contractual instruments such as tort or bilateral investment treaties, where no contract exists.[31] It is remarkable that the rules choose the term "to take account of" instead of "apply". The rules mean to indicate, e.g., that provisions, which are null and void must not be applied.[32]

17 The term "trade usage" is interpreted differently in various jurisdictions.[33] However, in the context of ICC arbitrations, UNIDROIT principles[34] or Art. 9(2) 2 CISG[35] will govern the interpretation.[36] Relevance of trade usages refers to the trade area as well as to a certain degree of firmness. Trade usages are relevant when they have been formalized to a certain extent and are widely accepted without having binding legal effect.[37] Examples are INCOTERMS, Uniform Rules for Documentary Credits and so on.[38]

18 Pourdet and Besson rightfully advocate that para. 2 applies for both arbitration in law and in equity.[39]

D. Paragraph 3

19 This paragraph permits the arbitrators to decide on the basis of fairness and equity. This is an opt-in provision, that the parties must enable the arbitrators to apply expressly.[40] This does not occur frequently.[41] Agreements to that effect are not assumed lightly.[42] As in French law, the designation must be unequivocal under Swiss law.[43]

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22 Bond/Paralika/Secomb, p. 350; Bühler/Jarvin, *2009*, para. 15.654; Bühler/Webster, para. 17-6; Reiner/Jahnel, para. 6 at Art. 17.

23 Bond/Paralika/Secomb, p. 350; Bühler/Jarvin, *2009*, paras. 15.657-15.658; Fry/Greenberg/Mazza, para. 3-755.

24 Craig/Park/Paulsson, p. 329; Bühler/Webster, para. 17-15; Fry/Greenberg/Mazza, para. 3-756.

25 Fry/Greenberg/Mazza, para. 3-752; Habscheid, *RIW 1998*, p. 423.

26 Bühler/Jarvin, *2009*, para. 15.655.

27 Poudret/Besson, para. 685.

28 Poudret/Besson, para. 687.

29 Poudret/Besson, para. 687.

30 Bühler/Webster, para. 17-61.

31 Fry/Greenberg/Mazza, para. 3-779.

32 Reiner/Jahnel, para. para. 9 at Art. 17.

33 Bühler/Webster, para. 17-62.

34 Bühler/Webster, para. 17-62.

35 Reiner/Jahnel, para. 10 at Art. 17.

36 Poudret/Besson, paras. 690-692, detailing general principles, trade usages and lex mercatoria.

37 Bühler/Jarvin, *2009*, para. 15.671.

38 Bühler/Jarvin, *2009*, para. 15.671.

39 Poudret/Besson, para. 689; but see Reiner/Jahnel, paras. 14-15 at Art. 17.

40 Lachmann, para. 3156.

41 Bühler/Jarvin, *2009*, para. 15.674; Born, p. 2238; Reiner/Jahnel, para. 12 at Art. 17.

42 Born, p. 2240; Fry/Greenberg/Mazza, paras. 3-786 and 3-790.

43 Poudret/Besson, para. 714.

While the rules are silent on this point, the jurisdiction of the seat and the likely enforcement country need to accept the *amiable composition* of the tribunal as well as the decision *ex aequo et bono* as in accordance with its public policy.[44] Enforceability is largely possible.[45] Annulment in Switzerland unlikely.[46] **20**

In general, both amiable composition and arbitration *ex aequo et bono*, are variations of the concept which allows the arbitrator some freedom from strict adherence to the rule of law.[47] According to Reiner and Jahnel they are similar concepts that are to be applied independent from national interpretations.[48] **21**

The *amiable compositeur* rule has French origins, it is contained in the French *Code de Procédure Civile*, Art. 1478. The exact meaning of Art. 21(3) is disputed. An ICC Task force dealt with the meaning (of Art. 17(3) which is now Art. 21(3)).[49] The exact powers of the arbitrators remain disputed.[50] It is clear, however, that even an *amiable compositeur* may not derogate from mandatory provisions.[51] Bühler and Jarvin state that even under *amiable compositeur*, para. 2 has to be taken into account and trade usages and contractual provisions observed.[52] Redfern and Hunter state the concept of equitable justice either means that the tribunal should apply relevant rules of law but ignore formalities; or that the tribunal should apply relevant rules of law unless the result is harsh in the case on point; or that the tribunal should decide on general principles of law; or that the tribunal can ignore all rules of law and decide as it sees fit.[53] **22**

In Switzerland *amiable compositeur* and decisions *ex aequo et bono* are separate concepts. The latter means simply the application of principles other than the rules of law, while *amiable compositeur*, the former requires the application of the rules of law in a moderated form.[54] **23**

In our opinion, the distinction between amiable composition and *ex aequo et bono* is purely academic.[55] This is because, firstly, the concepts are to be applied internationally and should not be interpreted in light of national notions, where they may have different meanings. Secondly, when arbitrators apply either one of these concepts they will not make a distinction between them when deciding equitably. It is submitted that the ICC Rules mention both terms in order to accommodate differing legal understandings that attach different meanings to these concepts. The previous rules only contained the concept of amiable composition. Poudret and Besson therefore argue, that the addition of *ex aequo et bono* proves that the ICC recognizes the distinctiveness of the concepts.[56] An arbitration clause using only one of the terms will not result in a different application of equity, so the result remains the same.[57] If one law permits amiable composition but not decisions *ex aequo et bono*, and the contract refers to the term not explicitly specified, this will not be beyond the law.[58] **24**

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44 Redfern/Hunter/Blackaby/Partasides, para. 3.201; Born, p. 2242.

45 Born, p. 2239, citing as example the European Convention, Art. VII(2).

46 Kaufmann-Kohler/Rigozzi, para. 651.

47 Kaufmann-Kohler/Rigozzi, para. 647; Born, p. 246; Poudret/Besson, para.710, who considers the concept of amiable composition as narrower and with a different approach.

48 Reiner/Jahnel, para. 13 at Art. 17.

49 See *ICC Arb. Bull. 2007/1*, pp. 51-63: *Amiable Composition and ICC Arbitration* (by L. Kiffer, president of the Task Force); cf. also *ICC Arb. Bull. 2007*/1, pp. 63-115: *Extracts from ICC Arbitral Awards relating to Amiable Composition*.

50 Born, p. 2240.

51 Bühler/Jarvin, *2009*, para. 15.676.

52 Bühler/Jarvin, *2009*, para. 15.678; Fry/Greenberg/Mazza, para. 3-788.

53 Redfern/Hunter/Blackaby/Partasides para. 3.199; Fouchard/Gaillard/Savage, p. 1502, supporting the latter notion.

54 Redfern/Hunter/Blackaby/Partasides, para. 3.196.

55 Fry/Greenberg/Mazza, para. 3-783.

56 Poudret/Besson, para. 711.

57 Craig/Park/Paulsson, para. 8.05, pp. 110-114, agreeing in essence; Fouchard/Gaillard/Savage p. 1502.

58 Poudret/Besson, para. 710.