Is International Commercial Arbitration an Autonomous Legal System?

A Thesis Submitted to

McGill University in partial fulfillment of
the requirements of the degree of

Master of Law

By

Farshad Sadafi Chaghooshi

Supervisor

Professor Fabien Gélinas

June 2013, Faculty of Law
McGill University
Montreal

To

My wife Azadeh

Whose constant support and help
made this project possible

Acknowledgements

I would like to express my gratitude to my supervisor Professor Fabien Gélinas for the valuable comments, suggestions, and involvement throughout the learning process that led to this Master's thesis. I felt encouraged every time we met. The guidance and support that I received from him were vital for the success of this project.

I would also like to thank Professor Rosalie Jukier, Associate Dean of Graduate Studies, for her kind reception and help during my LL.M. Program; without her encouragement and guidance in the research methodologies class, this research project would not have materialized.

My sincere thanks go to Professor Richard Janda, whose theoretical approach to law course established my background in legal theories. I also had the opportunity to audit some courses delivered by eminent specialists in international arbitration. Particularly, I feel truly indebted to Professor Frédéric Bachand for the information I obtained from his extrajudicial dispute resolution course and during the after-class discussions. Further thanks go to the Staff of Graduate Studies in Law and the McGill Law Library for their cooperation and administrative help.

I would as well like to express my great appreciation to Nickolas Shultz and Dr. Richard Cooper for helping me edit the thesis. Finally, I would like to thank my loved ones: my wife, who has supported me throughout the entire process by keeping me harmonious, and my parents whose contribution to my life is beyond words.

Abstract

In recent decades, the nature of international commercial arbitration has been transformed from a method of dispute resolution to an autonomous legal system. Globalization and a shift of power from states to private actors have resulted in the emergence of an international arbitration community that eventually produced this kind of transition.

This movement has generated a dynamic discussion over the legality and systematicity of the arbitral legal system. By applying various legal theories, scholars of different legal systems have analyzed the legality of the arbitral legal system. A few scholars have advocated the concept of this system based on a transnational legal positivism theory. In contrast, others, because of a lack of essential qualities of law and structural deficiencies in international arbitration, refuse to recognize it as an autonomous legal system.

The main objective of the present work is to study the major legal theories about the legality and systematicity of international commercial arbitration, and then to take an overview of the adverse and advantageous consequences of applying the concept of the arbitral legal system.

Résumé

Au cours des dernières décennies, l'arbitrage commercial international a subi de grandes transformations : longtemps utilisé comme simple méthode de résolution des différends internationaux, il est en voie de devenir un système de droit autonome. Avec la globalisation des échanges et des activités humaines et la décentralisation du pouvoir des États vers des acteurs privés, une nouvelle catégorie d'arbitres internationaux a fait son apparition, de nouveaux arbitres qui deviennent à leur tour des agents de changement.

La pluralité de leurs opinions a poussé ces nouveaux acteurs à se questionner sur la viabilité à long terme de la mise en place d'un nouvel ordre juridique arbitral. Diverses théories juridiques mises de l'avant par des experts issus de différents domaines du droit ont permis d'en étudier la légalité et la systématicité. Ce nouvel ordre juridique a ses défenseurs et ses détracteurs. Certains le défendent en invoquant la théorie positiviste du droit basée sur les règles de droit transnationales. D'autres refusent de le considérer comme un système autonome parce certaines règles de droit essentielles n'y sont pas définies et qu'il existe des lacunes structurelles flagrantes en arbitrage international.

Ce sont là quelques-unes des grandes questions qui seront débattues dans le présent ouvrage. L'auteur y fera d'abord l'analyse des principaux courants théoriques traitant de la légitimité et de la systématicité de l'arbitrage commercial international et de la mise en place d'un régime juridique dans ce domaine, pour se concentrer ensuite sur les avantages et les désavantages que sa reconnaissance en tant que système de droit autonome pourrait représenter.

Abbreviations

AAA	American Arbitration Association
Am J Comp L	American Journal of Comparative Law
Am J Juris	American Journal of Jurisprudence
Am J lnt'l L	American Journal of International Law
Am Rev Int'l Arb	American Review of International Arbitration
Am Rev lnt'l Arb	American Review of International Arbitration
Am U L Rev	American University International Law Review
Arb lnt'l	Arbitration International
Cambridge LJ	Cambridge Law Journal
Colum J Transnat'l L	Columbia Journal of Transnational Law
Duke J Comp & lnt'l L	Duke Journal of Comparative & International Law
EJIL	European Journal of International Law
Harv Int'l LJ	Harvard International Law Journal
Harv L Rev	Harvard Law Review
HKIAC	Hong Kong International Arbitration Centre
ICC	International Chamber of Commerce

ICSID	International Centre for settlement of Investment Disputes
IBA Guidelines	International Bar Association Guidelines on Conflicts of Interest in International Arbitration
IBA	International Bar Association
ICLQ	International & Comparative Law Quarterly
ILM	International Legal Materials
JDI	Journal du droit international
J Int'l Arb	Journal of International Arbitration
J Legal Pluralism	Journal of Legal Pluralism and Unofficial Law
Law & Pol'y lnt'l Bus	Law and Policy in International Business
LCIL	London Court of International Arbitration
Leiden J lnt'l L	Leiden Journal of International Law
lnd J Global Legal Stud	Indiana Journal of Global Legal Studies
lnt'l Law	International Lawyer
Loy LA lnt'l & Comp LJ	Loyola of Los Angeles International & Comparative Law Review
McGill LJ	McGill Law Journal
Mich J Int'l L	Michigan Journal of International Law
Mont L Rev	Modern Law Review
New lJ	New York Law Journal

NGO	Non-governmental Organization
Nw UL Rev	Northwestern University Law Review
NYUJlnt'l L & Pol	New York University Journal of International Law & Politics
Oxford J Legal Stud	Oxford Journal of Legal Studies
S Cal L Rev	Southern California Law Review
San Diego L Rev	San Diego law review
SIAC	Singapore International Arbitration Centre
Stan L Rev	Stanford Law Review
Theor lnq L	Theoretical Inquiries in Law
TNC	Trans-national Corporation
Transnat'l L & Contemp Probs	Transnational Law and Contemporary Problems
Tul L Rev	Tulane Law Review
UNCITRAL	United Nation Commission on International Trade Law
Unif L Rev	Uniform Law Review
Vand J Transnat'l L	Vanderbilt Journal of Transnational Law
Yale JL&T	Yale Journal of Law & Technology
Yale LJ	Yale Law Journal

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INTRODUCTION

In recent decades, the nature of international commercial arbitration has been transformed from a method of dispute resolution to an autonomous legal system. Globalization has brought new dimensions to the practice of law by sweeping across borders. It has fostered international commercial arbitration as a reliable mechanism to settle international commercial disputes. The globalized economy has shifted the power from states to private actors and created a global communication network that eventually helped the formation of the global arbitration community, the prerequisite for the foundation of the arbitral legal system.

Cross-border legal conflicts and the clash of legal systems are inevitable by-products of international exchanges. The criticism is that national laws have not been fully capable of dealing with modern transnational issues because they are designed for domestic disputes and are not adequate to answer many complicated international cases; this is particularly the situation when a non-developed national law is meant to govern the case at hand.[1] For this reason, given that transnational conflicts demand supranational solutions, new demands arise to resolve international commercial disputes in a truly international process.

To fulfill these demands, trans-national and trans-systemic practices of law have proliferated in recent decades. Policy-making and judicial practices of law in international commercial contexts have increased. Activities of the

[1] In order to determine the applicable law, national courts normally use the classical conflict of law rules or they may recognize parties' choice of law.

transnational institutions and codification movements have provided substantive and procedural rules and policies to govern international business activities.

Merchants have also fostered mechanisms to resolve possible legal conflicts.[2] Among them, arbitration has received considerable attention. The advantages[3] of international arbitration have persuaded merchants to trust arbitration as an efficient and neutral method. Institutionalized and systematic practices of arbitration have produced procedural and substantive norms and customs that, after constant practice, have turned into universally accepted principles.[4]

The history of international commercial arbitration shows that it has been constantly going through a process of transformation in response to the needs of the global market. The international arbitration community has been conceptualizing arbitration[5] in various forms to better serve the arbitration users.

In the first stage, states were hostile to arbitration and reluctant to hand over part of their sovereignty to a private tribunal.[6] By ratifying the Convention

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[2] Arbitration, mediation, conciliation, negotiation are mechanisms of conflict resolution that are used for resolving international business disputes.

[3] The most important advantages of international commercial arbitration include: being a binding mechanism, being neutral, and having a trans-national and trans-systemic legal framework. See Martin Domke, *Commercial Arbitration* (New Jersey: Prentice-Hall, 1965).

[4] See Gabrielle Kaufmann-Kohler, "Globalization of Arbitral Procedure" (2003) 36:4 Vand J Transnat'l L at 1313. ["Globalization of Arbitral Procedure"]

[5] Hereinafter, whenever the term arbitration is used, it refers to international commercial arbitration.

[6] Gary Born, *International commercial arbitration* (Austin: Wolters Kluwer Law & Business, 2009) at 7-63.

on the Recognition and Enforcement of Foreign Arbitral Awards[7] (New York Convention) in 1958, the global society recognized the growing importance of arbitration. This was a big and successful step towards the reconciliation of public and private justice. However, some states were very conservative in granting full autonomy to arbitration. Other states have given a significant role to the place of arbitration under the influence of legal theories such as the territorial theory and legal positivism. International commercial arbitration has been considered part of the legal system of the state where an arbitral tribunal has its seat. It also has been argued that the awards' legal value is derived from a national legal system. From an extreme point of view, some scholars, such as F. A. Mann, even deny the existence of international commercial arbitration and believe that there exists only national arbitration:

> [T]he phrase is a misnomer. In the legal sense no international commercial arbitration exists. Just as, notwithstanding its notoriously misleading name, every system of private international law is a system of national law, every arbitration is a national arbitration, that is to say, subject to a specific system of national law.[8]

Practical concerns and involvement of several national legal systems in the processes of arbitration have caused some scholars to take the pluralistic approach

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[7] *Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, June 10, 1958, 330 U.N.T.S. 3; 21 U.S.T. 2517. [New York Convention]

[8] FA Mann, "Lex facit arbitrum" in Pieter Sanders, ed, *International arbitration. Liber amicorum for Martin Domke* (The Hague: Martinus Nijhoff, 1968) at 159; cited in Emmanuel Gaillard, *Legal theory of international arbitration* (Leiden: Martinus Nijhoff Publishers, 2010) at 18 [*Legal Theory*]; see ibid at 15; also see Jan Paulsson, "Arbitration in three dimensions" (2011) 60:2 ICLQ 291 at 293.

and to delocalize arbitration.[9] According to the pluralistic approach, arbitration does not have a place; therefore, all national legal systems that have a connection to arbitration cases should be taken into consideration.[10]

Finally, given the vast and systematic practice of arbitration and emergence of non-state laws, some scholars have tried to give autonomy to arbitration. They have taken different approaches to autonomy and theorized arbitration in various forms. For instance, Emmanuel Gaillard has introduced arbitration as the "transnational comparative method of dispute resolution". According to this approach, transnational law is not a set of rules, but a comparative method to choose a rule that is generally accepted by the international arbitration community.[11]

> The other approach to defining the contents of transnational law is to view transnational law as a method of decision-making, rather than as a list. This approach consists, in any given case, of deriving the substantive solution to the legal issue at hand not from a particular law selected by a traditional choice-of-law process, but from a comparative law analysis which will enable the arbitrators to apply the rule which is the most widely accepted to a rule which may be peculiar to a legal system or less widely

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[9] Jan Paulsson has defined the delocalization of arbitral awards as the possibility of enforcing the arbitral awards annulled in the country of origin. "'Delocalization' refers to the possibility that an award may be accepted by the legal order of an enforcement jurisdiction whether or not the legal order of its country of origin has also embraced it". See Paulsson, at 298.

[10] See ibid at 96-300; see also Gaillard, "Legal Thepory" *Supra* note 8 at 24-25.

[11] Emmanuel Gaillard, "Transnational Law: A Legal System or a Method of Decision Making?" (2001) 17:1 Arb lnt'l 59. ["Transnational Law"]

recognized.[12]

In a more recent attempt, one that has attracted more attention, arbitration has been conceptualized as an "arbitral legal order". Emmanuel Gaillard, who is one of the leading figures in international arbitration, revived[13] the expression and initiated a series of debates about the concept of an arbitral legal order. According to him, the arbitral legal order exists because some arbitrators and practitioners intuitively perceive and comprehend such an order. The arbitral legal order does not derive its validity from a national legal system, and arbitrators do not decide cases on behalf of states. Instead, the source of their powers to adjudicate is derived from the transnational arbitral legal order. Gaillard continues by noting that as a result of the fact that there is no generally accepted definition of the arbitral legal order, we should consider the main characteristics of a legal order. According to him, such a legal order should be effective, complete and coherent, capable of reflecting its source, and having appropriate subjects and organs.[14]

The theory of the arbitral legal order has generated a series of discussions about the existence and validity of the arbitral normative order. It has also

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[12] Ibid at 63-64.

[13] The term "arbitral legal order" entered legal terminology in the mid-1990's. Professor Loquin introduced the idea of an "anational legal order" when theorizing a transnational law that could be applied to arbitration cases. See Eric Loquin, "L'application des règles nationales dans l'arbitrage commercial international", in L'apport de la jurisprudence arbitrale, ICC Paris 1986, 87, footnote 95. In 1993, Professor Daniel Cohen used the expression "arbitral legal order" in his book "*Arbitrage et société*". See Daniel Cohen, *Arbitrage et société* (Paris: Librairie générale de droit et de jurisprudence, 1993) at 21. Other scholars have also used the same expression; see Gaillard, "Legal Thepory" *supra* note 8 at 38-39.

[14] Emmanuel Gaillard, "L'ordre juridique arbitral : réalité, utilité et specificité: conference commemorative John EC Brierley" (2010) 55:4 McGill LJ at 891 ["L'ordre juridique"] ; Emmanuel Gaillard, "The Representations of International Arbitration" (2007) 238 67 NYLJ at 35-67. ["The Representations"]

initiated dynamic discussions over the legality and sytematicity of the arbitral legal order. By implementing various legal theories, scholars of different legal systems have analyzed the legality of the arbitral legal order. A few scholars have advocated the concept of an arbitral legal order based on the transnational legal positivism theory. In contrast, others, because of a lack of the essential qualities of law and structural deficiencies in international arbitration, refuse to recognize it as an autonomous legal order.

The objective of this research is to assess the arbitral legal system with various theories of law, including the theory of natural law, legal positivism, and social scientific theories of law. I will attempt to encourage the international arbitration community to conceive of arbitration as an autonomous legal system. This thesis, therefore, attempts to provide theoretical grounds to support both the legality and systematicity of arbitration.

I have chosen "arbitral legal system" instead of other similar terms because the elements and characteristics of the modern arbitration and global arbitration society depict it as an independent legal system. In order to choose the appropriate terminology, it is important to distinguish apparently similar terms that are used often interchangeably. For the purpose of this research, I will use "arbitral legal system" instead of "arbitral legal order", "the universally accepted arbitral principles", "autonomous transnational legal order", "transnational arbitral rules", and "arbitral normative order".

I have chosen the word "legal" because it distinguishes social norms from legal norms. In other words, it distinguishes better the social conventions from the binding norms backed by sanctions. Moreover, it fits better with the purpose of

my thesis, which is to justify that transnational arbitral rules deserve to be called law.

In addition, I have selected "system" over "order". Although, some authors have used these terms interchangeably, it seems that "system" reflects the reality of modern international commercial arbitration more accurately. Also, it reflects better the consistency of arbitral decisions ("systematicity") and the dynamicity of arbitral laws ("systematization").[15]

To address the objectives of this thesis, first, I will study the factors impacting the formation of the arbitral legal system and signs of its validity (subject of chapter one). Second, I will analyze the legality and systematicity of the arbitral legal system based on the traditional, modern and post-modern concepts of law and legal system theories (subject of chapter two). Finally, I will try to analyze the positive and negative practical consequences of the application of the concept of the arbitral legal system (subject of chapter three).

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[15] For the distinction between system and order see Michel Van De Kerchove & François Ost, *The legal system between order and disorder* (Oxford: Oxford University Press, 1993) at 4-5.

CHAPTER ONE
The Existence of an Autonomous Arbitral Legal System

1) Introduction

In order to answer the question regarding the existence of an arbitral legal system, one must first define its components and afterwards determine the systematicity among those elements, which is the subject of the next chapter (chapter two). However, before such an explanation, it is important to discuss the main factors contributing to the formation of an autonomous arbitral legal system and to identify some practical signs that lead one towards acknowledging the existence of an independent arbitral legal system. Although, these signs are not independently sufficient to lend credibility to arbitration as an independent legal system, they at least show that international commercial arbitration is seen as capable of guaranteeing justice in international commercial relationships.

Therefore, in the first part of this chapter, I will discuss how globalization, as the most important factor, has contributed to the formation of the autonomous arbitral legal system. In the second part, I will argue for some significant indications that signal the existence and validity of such a system.

2) Impact of Globalization on the Formation of an Arbitral Legal System

Globalization has accelerated the pace of the development and transformation of international commercial arbitration in different ways.

Globalization is a complex multi-dimensional phenomenon that has been defined in many ways, depending on the context. The study of globalization processes is a multi-disciplinary one. The concept can be defined narrowly by focusing on one discipline, for instance communications studies or economics. It can also be defined broadly, taking account of all the disciplines involved in the study of the processes of globalization. For the purpose of this research, I will take the broad definition of globalization because I believe that globalization is a dynamic process that is the result of interactions among many different factors.

Nayef R.F. Al-Rodhan and Gérard Stoudmann conducted an interesting analytical study about the definition of globalization. After collecting the important definitions of globalization in different disciplines, they adopted common denominators and concluded with a comprehensive definition. According to them, "Globalization is a process that encompasses the causes, course, and consequences of transnational and trans-cultural integration of human and non-human activities."[16] According to this definition, as it relates to international commercial arbitration, globalization is an evolving process through which transnational integration and exchange occur in several respects, including cultural, technological, economic, legal, and political.

The integration of the world's economy has led to a global economy with new legal needs. The growth of cross-border exchanges and clash of legal traditions and systems have challenged the traditional order in international law.

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[16] Nayef RF Al-Rodhan, *Definitions of Globalization, A Comprehensive Overview and a Proposed Definition* (Geneva: Geneva Centre for Security Policy, 2006) at 5.

In the process of globalization, states' sovereignty has been affected noticeably by emerging private sectors to the extent that power has shifted from states to non-state actors. States have had to give up part of their sovereignty in favor of global market forces. Global market theories and principles, such as free trade, have further limited states' power in the modern globalized economy. The emergence of international non-state entities has led to the creation of new norms and standards outside governments. In these processes, technological innovations have played an important role by providing networking opportunities for the entire world to exchange information.

Globalization, in turn, has transformed international commercial arbitration from different perspectives. It caused arbitration to emerge as a reliable conflict resolution mechanism. It also impacted how the international arbitration community conceives international commercial arbitration. The globalized economy has generated new demands of arbitration and in order to satisfy them, arbitration had no choice but to undergo transformation. In addition, the rise of private actors and entities in the international environment has limited the power of states and has forced them to adopt a liberal approach towards international commercial arbitration. The institutionalization of arbitration, the publication of arbitral awards and scientific opinion, communication facilities and massive online databases have made the arbitrators and arbitration's users well connected to each other and have led them towards the creation of the international arbitration community.

In the next three parts, I will discuss the major impacts of globalization on international commercial arbitration in more detail.

A. Globalized economy and international commercial arbitration: mutual interaction

The globalized economy has played two main roles in the transformation of international commercial arbitration. The first is to promote the widespread use of international commercial arbitration. The second is to force arbitration to be transformed into a more effective mechanism based on the new demands and market reality.

Merchants have chosen arbitration as the most effective dispute resolution mechanism to cope with the economic risks and legal uncertainty of cross-border exchanges.[17]

Globalization has integrated the world's economy. Merchants around the globe have found domestic markets saturated; and, therefore, to expand their businesses, have stepped beyond borders to enter the ever-growing global competition. By going through the statistics, one can see how dramatic the world's economic growth is. One sees the emerging economy all over the world, from Asia, the Middle East and Europe to South and North America. For instance, the total amount of exports from China in 1982 was around US/$21 trillion. This amount quadrupled in 1992, and reached US/$325 trillion in 2002.[18] China is not the only economy that has flourished dramatically. Brazil's total amount of

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[17] Katherine L Lynch, *The forces of economic globalization, challenges to the regime of international commercial arbitration* (The Hague: Kluwer Law International, 2003) at 3.

[18] Data extracted from the World Bank databases. World Development indicators, Merchandise Exports by the Reporting Economy online: World Bank <http://data.worldbank.org/indicator/TX.VAL.MRCH.WL.CD>.

exports has doubled in each decade since the 1980s, and Turkey's total amount of exports has tripled in the same period.

Chart 1: Total amount of exports in a specific period of time in some countries:

Country	TAE* 1982	TAE 1992	TAE 2002
China	21 Trillion**	85 T (+400%)	325 T (+382%)
Brazil	20 T	37 T (+185%)	60 T (+162%)
Turkey	5 T	14 T (+280%)	36 T (+250%)
France	96 T	236 T (+240%)	331 T (+140%)
Canada	71 T	133 T (+187%)	259 T (+180%)

* Total amount of export. ** All amounts are in US dollars and in trillions.

Bearing in mind the very rapidly growing world economy, the question that arises here is whether or not there is a relationship between law and economic development. Do classic solutions such as domestic legal systems or conflict of law rules suffice to guarantee business activities? Does a flourishing global economy need a new method or independent legal system to reach that objective?

If the answer to the latter question is positive, then what characteristics should that legal system have?

Large numbers of research projects done by different groups have proved fairly clearly that law both negatively and positively impacts the economy. Generally, comparative research studies with different approaches have demonstrated that efficient legal systems and effective sets of rules, as well as efficient institutions, lead to economic development.[19]

A study group at the World Bank conducted series of empirical studies in more than 150 countries.[20] The group compiled a database of "governance indicators" such as "rule of law" and "regulatory burden" and analyzed their relationship with economic outcomes. The study showed that there is a relationship between efficient governance and economic developments.

In another study, Kenneth Dam concluded that legal origins and rule of law significantly matter to economic development. He pointed out that a better procedural law and an efficient judiciary lead to economic growth. He argues that bad substantive laws such as contract and property law are the main obstacles for economic growth in some developing countries.[21]

Despite the fact that all the above-mentioned research studies are about domestic legal systems and state's institutions, one can extrapolate and be

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[19] Daniel Sokol has categorized these research studies according to their approaches in his 2010 article. Daniel D Sokol, "Law and Development: The Way Forward or Just Stuck in the Same Place?" (2010) 104 NWUL Rev 238.

[20] Daniel Kaufmann, Aart Kraay & Pablo Zoido, *Governance Matters*, vol. 2196 (Washington: The World Bank, 1999), online: http://wbi.worldbank.org/wbi/topic/governance.

[21] Kenneth W Dam, *The Law-Growth Nexus: the Rule of Law and Economic Development* (Washington, D.C.: Brookings Institution Press, 2006).

confident that economic development is not possible without an efficient legal framework to protect business. Particularly, in the global economic context, with respect to legal complexity and uncertainty and the economic risk of massive cross-border exchanges, the global business community needs to develop a reliable and independent legal system to guarantee its activities.

Therefore, international law practitioners have tried to provide the business community with new solutions to create legal certainty. Nevertheless, those innovations have not been very successful, and the entire community finds them rather obsolete. These legal solutions are mostly within the plural legal frameworks and are based on party autonomy. The two best-known solutions are: 1) choosing applicable substantive law to govern the legal relationship (for instance, the Convention on the Law Applicable to Contractual Obligations 1980 that was replaced by the Rome I regulation 2008) and 2) determining the competent court to decide the case (for example, the Hague Convention on Choice of Court Agreements 2005). Owing to some practical obstacles and limited applicability, neither of these two solutions can achieve the establishment of a just legal framework to resolve international commercial disputes.

The Choice of Court Convention is designed to recognize party autonomy in choosing a neutral jurisdiction to decide the case at hand and to facilitate the enforcement of foreign judgments. It helps parties choose a fair and effective jurisdiction to decide the case; however, some practical obstacles prevent the Choice of Court Convention from being an attractive mechanism to settle international disputes. For instance, Choice of Court is limited in scope and has excessive jurisdictional exceptions. In addition, the grounds for refusing

enforcement of the courts' decision are unclear, given that they are different in different jurisdictions.[22] Parties are not free to choose their procedural law. They are also indirectly prevented from choosing a set of transnational laws to be applied in their case since some national courts will not recognize such a law.

Due to these and other shortcomings, it seems that any attempt within the plural legal system would not be capable of satisfying the needs of international business activists. Therefore, it appears that they require a suitable conflict resolution mechanism that both reflects the needs of the modern global market (for instance, the need for a neutral, impartial, and transnational legal framework) and is relatively independent from state interference.

Probably, it was these requirements that made international commercial arbitration more attractive in comparison to other mechanisms. The flexibility of arbitration allows parties to design their legal framework. Parties are able to choose procedural laws, a chance of which they may be deprived in national courts, given that procedural law comes within the national court. They may choose a transnational law as an applicable law, which is not recognized in national courts. To support this claim, it is worth mentioning that the results of a survey done by Price Waterhouse Cooper about business corporations' attitudes towards arbitration in 2006, 2008, and 2010 showed that 73% of participants preferred arbitration to international litigation.[23] The survey also demonstrated

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[22] Masato Dogauchi & Trevor C Hartley, *Preliminary Draft Convention on Exclusive Choice of Court Agreements* (The Hague: Conference on Private international Law December, 2004) online: <http://www.hcch.net/upload/wop/jdgm_pd26e.pdf>.

[23] "International arbitration: Corporate attitudes and practices 2006" online: Price Waterhouse Cooper <http://www.pwc.be/en_BE/be/publications/ia-study-pwc-06.pdf>

that 86% of participants were satisfied with arbitration after using it.[24] Furthermore, the survey revealed that 68% of surveyed corporations have a policy regarding arbitration; and some industries, such as insurance, gas and oil, and transportation, tend to put arbitration clauses in their agreements by default.[25]

The relation between law and economic development is mutual. The widespread use of international commercial arbitration has made it transform itself according to the needs of the market. Perhaps, the most important transformations are, first, the shift in how international arbitration operates in the modern era and, second, its move towards independence from states. As a result of market forces, arbitration has been institutionalized over decades, and the institutionalization of arbitration has accelerated in recent decades. Many arbitral institutions have been established and the old institutions have revolutionized their case management's style and procedures. Some examples of arbitration institutions are the International Chamber of Commerce (ICC), American Arbitration Association (AAA), London Court of International Arbitration (LCIA), Hong Kong International Arbitration Centre (HKIAC), and Singapore International Arbitration Centre (SIAC). Because of the logistic services these institutions provide for parties, use of institutional arbitration has increased. For instance, requests for arbitration filed with the ICC have increased more than 30

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[24] "International arbitration: Corporate attitudes and practices 2008" online: Price Water house Cooper, <http://www.arbitrationonline.org/docs/IAstudy_2008.pdf>.

[25] "2010 International Arbitration Survey: Choice in International Arbitration" online: Price Water house Cooper <http://www.arbitrationonline.org/docs/2010_ International Arbitration SurveyReport.pdf>.

percent in 12 years.[26] In addition, institutional arbitration has made it possible to collect, classify and, publish substantial arbitral awards. As a result of the publication of selected arbitral awards, numerous opinions and doctrinal ideas have been generated in the arbitration domain.

One can conclude that as a result of the mutual interaction between law and economic development, international arbitration has shifted from a mere dispute resolution method to a more sophisticated self-organized legal system that tends to emancipate itself from any dependence on states and domestic laws.

B. Shift of power from states to private sectors

For many years, states have been the only dominant players in shaping international law. All the relevant sources of international law were derived from sovereign state activities in the form of bilateral or multilateral treaties or customary law.[27] As a result of the globalized economy, the importance of political borders has diminished and the sovereignty of nation-states has been challenged. Many powerful transnational non-governmental institutes and organizations have emerged. Multinational and transnational companies dominate the world's economy. In addition, the age of information explosion has provided the entire world with communication facilities and massive online databases that

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[26] According to the ICC statistics, in 1999, 520 requests for arbitration were filed. This number increased to 759 requests in 2012. Online: <http://www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Introduction-to-ICC-Arbitration/Statistics/>.

[27] *Statute of the International Court of Justice, June 26, 1945* (1945). art. 38(1) online: <http://www.icj-cij.org/documents/?p1=4&p2=2&p3=0>.

have made it easier than ever to share ideas as well as to access information. Technological advances and public access to them have increased the role of non-state sectors in shaping new legal orders. With respect to these consequences of globalization, the issue here is: whether and to what extent globalization has shifted the traditional global order? How has it affected states' sovereignty? And, finally, how does it transform international commercial arbitration?

One answer could be that the globalized economy does not affect states' sovereignty at all. The commentators in this category admit that the globalized economy has affected the quality of practicing sovereignty, but they refuse to admit that the nation-state's authority has diminished.[28] Many scholars believe however, that the globalized economy has led to a redistribution of power in the international environment and has caused a shift in power from the state sector to the private sector. Jessica Mathews has described this notion very well. She describes the global economy as "[t]he most powerful engine of change in the relative decline of states and rise of non-state actors."[29]

Globalization has limited governments' sovereignty domestically and internationally. Domestically, globalization, as Till Müller puts it, has attacked states' three traditional practices of sovereignty, namely; their legislative, executive, and judicial powers. He emphasizes the role of transnational corporations and non-governmental organizations in influencing the policy-

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[28] See Lynch, *sura* note 17 at 38.

[29] Jessica T. Mathews, "Power Shift" (1997) 76 Foreign Affairs 50 at 51.

making process.[30] Furthermore, it is said that states do not make new policies. Instead, the global market is generating de facto rules, and governments merely need to adopt them in the process of adapting themselves to globalization.[31]

In the global context, states are no longer the only main players. The private sector, including international institutions, transnational corporations, and non-governmental organizations, is playing a significant role in shaping the global order. Müller states that international customary law has turned into "transnational customary law" not limited to governments' activities; it is "dependent on the customs of the international community at large."[32]

This shift of power in international society has had some major legal consequences. First, the involvement of the private sector in the global law-making process has altered the way we look at "law" in the international context and international law generally. Globalization has changed the traditional meaning of law and broadened the traditional sources of international law. "Law" is not concentrated in states' official organs anymore. As Paul Berman explains, "scholars are increasingly coming to recognize, there is no need to see law as necessarily encapsulated only by formal government acts."[33] Professor Janet Koven Levit, by giving some examples, demonstrates how "informal and unofficial communities" have taken over the traditional responsibilities of states.

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[30] Till Müller, "Customary Transnational Law: Attacking the Last Resort of State Sovereignty" (2008) 15:1 lnd J Global Legal Stud 19.

[31] Mathews, *supra* note 29 at 51.

[32] Müller, *supra* note 30 at 21.

[33] Paul Berman, "From international law to law and globalization" (2005) 43:2 Colum J Transnat'l L 485 at 493.

She describes how this "bottom-up lawmaking" process as a common practice of non-state sectors, by means of communication and information exchanges, establishes rules governing specific professional activities.[34] Second, the shift of power has caused the private sector to act more autonomously and independently from national states. Non-government organizations and institutions and transnational companies have had the chance to develop the capacity to create policies and standards for their own. They also have developed the mechanisms to enforce their rules. In addition, because of the fact that they are interacting with each other, they have needed to develop a networking system in order to balance their regulations according to the global environment. This broad practice of authority has made them more sophisticated than ever.

The relationship between states and NGOs and TNCs has often been problematic. States have been reluctant to give up their sovereignty, and they have been unwilling to recognize the pivotal roles of NGOs and TNCs. However, they are gradually being forced to recognize the private sector's role in international law. This is perhaps due to the fact that they need to cooperate with the private sector. Some states, due to political, financial, and inefficiency obstacles, are not able to solve all their international problems, or they may not even be interested in doing so. Therefore, cooperation between states and the private sector could benefit both sides.[35] International commercial arbitration is no exception in this power struggle between the private sector and states. Since the time when

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[34] Janet Koven Levit, "Bottom-Up Lawmaking: The Private Origins of Transnational Law" (2008) 15:1 lnd J Global Legal Stud 49.

[35] Müller, *supra* note 30 at 23-24.

international commercial arbitration emerged, states have gone through different stages to accept the significant role it has come to play. First, national courts in the past played the main role in international commercial cases. Thus, states were reluctant to fully validate international arbitration. Then, after signing the New York Convention (The 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards), states started to recognize arbitration as a private mechanism of resolution of international conflicts. This, in turn, made room for the rise of non-governmental sectors to dominate the international arbitration and to shape their own legal order. The growth of international organizations and corporations, as well as the institutionalization of international commercial arbitration, has facilitated the movement towards the replacement of public law by private law.[36]

The emergence of institutionalized international arbitration and the creation of transnational arbitration rules, in addition to the development of transnational substantive rules, have forced national legal systems to take a liberal approach in dealing with international arbitration. In recent legislative reforms, states have adopted non-interventionist policies in their arbitration laws. They have established *laissez-faire* judicial review; and this has provided an excellent opportunity for international arbitration to rule its own domain through its specific legal framework, which is relatively independent from states' authority.[37]

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[36] Alan Scott Rau, "Contracting out of the Arbitration Act" (1997) Am Rev lnt'l Arb 225 at 259.

[37] William W Park, *Arbitration of international business disputes, studies in law and practice* (Oxford; New York: Oxford University Press, 2006) at 16; Yves Dezalay & Bryant G Garth, *Dealing in virtue, international commercial arbitration and the construction of a*

C. Global communication and the creation of the international arbitration community

Intense interaction between and among members of the international arbitration community has caused major changes in the nature and characteristics of international commercial arbitration. Generally, the decision-making process in international arbitration cases is the result of intensive interactions among arbitration community members globally. In this process, interaction among and between arbitrators, lawyers, parties' counselors, scholars, and merchants as constituents of this diverse legal society has been invaluable for the development and transformation of the area.

The role of international legal communication and social networking in this transformation processes is considerable. Systematic exchanges of ideas can create new norms and customs as well as reduce the gaps and differences in international arbitration practices and doctrines. Networks also prevent practitioners from divergent interpretations, correct inefficient practices, and adjust the regulations according to the international nature of arbitration.[38] Besides, such intense legal interactions will eventually turn into more sophisticated networks of ideas that can transform the field. In this respect, globalization and, in particular, the emergence of a global economy has speeded

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transnational legal order (Chicago: University of Chicago Press, 1996) at 34; Lynch, *sura* note 17 at 121.

[38] On social networking of international judges, see Daniel Terris, Cesare PR Romano & Leigh Swigart, "Toward a community of international judges" (2008) 30:3 Loy LA lnt'l & Comp LJ 419 at 420. Regarding how International judges are forming a global community, see Anne-Marie Slaughter, "A global community of courts" (2003) 44:1 Harv Int'l LJ 191 at 219.

up the transition of arbitration from a rudimentary to a more mature state in various ways as described below.

First, competition among the international arbitration community has resulted in international commercial arbitration becoming institutionalized and rationalized. The emerging global economy has created competition among international arbitration community, including law firms and institutions of international commercial arbitration. For purposes of marketing, they try to provide better service in to order to attract more clients. They engage in more intense legal discussions and contribute more to the community in order to stay in the market. As some scholars have noted, transformation of arbitration occurs in this global dialectical environment through the conflicts of old practitioners versus new generations as well as those of academic scholars versus practitioners.[39] This kind of competition promotes law in international mercantile relations and builds "the legitimacy and credibility of international legal practices and international institutions."[40] In addition, owing to the competitive environment, many international arbitration institutions like ICC have been established to facilitate and administer international arbitration. This, in turn, has caused the practice of international arbitration to become institutionalized and rationalized.[41] In the long run, competition among international arbitration

[39] Dezalay & Garth, *supra* note 37 at 42.

[40] Ibid at 33.

[41] Ibid at 57.

community and rationalization of the system have transformed international arbitration into a legitimate and decentralized transnational private justice.[42]

Second, use of arbitration for resolving the conflicts arising out of North-South commercial relationships has caused alterations in the nature of international arbitration. Particularly, they have transformed arbitration to adopt a transnational and trans-systemic framework so as to remain as neutral as possible.

In the globalized economy, more than ever, industrialized countries have commercial ties with the so-called developing countries, most of which are exporters of raw materials and importers of industrial goods and services. In any conflict, developed states try to guarantee their benefits and protect their investments. On the other hand, developing countries are worried about their national interest or being in a weak position to protect their public interests. Bearing in mind that most of the developing countries are ex-colonial territories and have a history of exploitation by foreign powers, the economic and political imbalances of parties have led both sides to choose the best mechanism to resolve conflicts. The specialty and complexity of the situation also have brought about alterations in the entire field.

The reason why international arbitration has been chosen as the most desirable mechanism for resolution of North-South conflicts is obvious. It is an "international" solution that at the same time does not conflict with nation-states' sovereignty. International arbitration is not an international framework superior to the nation-state. This is a neutral method of resolving disputes that is operating

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[42] Ibid.

with internationally accepted principles and within a transnational and trans-systemic legal framework.

One of the most important alterations is the possibility of choosing an anational body of law like general principles, or *lex mercatoria,* to be a governing type of law in international commercial arbitration. Since parties with different levels of political and economic power seek a neutral body of law, some countries have prohibited public entities from choosing a foreign law to govern a legal relationship.[43] Moreover, arbitral awards that have constructed their reasoning on the grounds of general principles of law or other non-state bodies of law further emphasizes the legitimacy of such a transnational body of law.

Finally, the influence of the business sector on international commercial arbitration and its specific expectations have altered the nature of international commercial arbitration. It should be borne in mind that the ultimate goal of international commercial arbitration is to serve the commercial communities.[44] It is reasonable if the powerful international corporations and merchants tend to have control over the mechanism to resolve their own disputes.[45] Merchants, in order to regulate their conflicts by themselves and to limit states' interference in their affairs, established the Court of Arbitration of International Chamber of Commerce in 1923. They developed their own body of law through various means, such as regulating codes of conduct or business standards and terms. They also chose their trusted arbitrators and experts. They insist on their expectations

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[43] Ibid at 89.

[44] Fabien Gélinas, "Arbitration and the challenge of globalization" (2000) 17:4 J Int'l Arb 117 at 117.

[45] Dezalay & Garth, *supra* note 37 at 118.

from lawyers and the international arbitration system by tailoring the arbitration framework and otherwise through the process of arbitration.

To conclude, it seems that perpetuation of the dialectic among global arbitration community and with the market has constantly transformed international commercial arbitration. As Professor Dezalay states: "international commercial arbitration can be transformed or even replaced because it is part of a larger international market of commercial or business disputes, and the market is inevitably unstable."[46] Interactions between different generations of practitioners among themselves and with the market, on one side, and with scholars, on the other side, have brought different perspectives into the arbitration process. As a result of these interactions, it is possible to observe an increased use of transnational bodies of law in arbitration processes and the institutionalization and systematization of international arbitration. Systematization of international commercial arbitration, eventually, leads it to become delocalized and independent from the legal system of its home seat or other involved states.

3) Signs of the validity of the arbitral legal system

In the previous section (section1), I pointed out some significant changes in international commercial arbitration caused by the globalized economy. In this part, I will try to demonstrate that the transformation of international commercial arbitration has impacted real practice. I attempt to show that the international arbitration community has acknowledged the detachment and independence of

[46] Ibid at 312.

international commercial arbitration from state legal systems in various ways. This phenomenon has also been reflected in states', parties', and lawyers' daily practice as well as in discussions among scholars. It has had an influence on international treaties, national statutes, and courts' decisions. These signs of recognition by the international arbitration community are affirming that international commercial arbitration is fully capable of being an independent legal system.

A. The New York Convention and the source of the validity of international commercial arbitration

The 1958 "Convention on the Recognition and Enforcement of Foreign Arbitral Awards,"[47] adopted in June 1958, is the most successful treaty in the arbitration field.[48] According to Articles II and III of the Convention, contracting states must recognize international arbitration agreements and recognize and enforce foreign arbitral awards. The Convention also lists limited and exhaustive grounds for refusing recognition and enforcement of awards. Therefore, it is clear that the Convention was established primarily on the basis of a "pro-enforcement principle."[49] Particularly, article V (1) (e) of the Convention allows member states

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[47] It will be called the New York Convention for the rest of this thesis; "Convention on the Recognition and Enforcement of Foreign Arbitral Awards", June 10, 1958, 330 U.N.T.S. 3; 21 U.S.T. 2517.

[48] For list of contracting states consult online: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.htm;and at http://www.newyorkconvention.org/contracting-states/list-of-contracting-states.

[49] Bernard Hanotiau, "International Arbitration in a Global Economy, The Challenges of the Future" (2011) 28:2 J Int'l Arb 89 at 91.

to enforce an arbitral award that was annulled by the court of the seat.[50] This means that annulment of an arbitral award by the seat does not necessarily render the award invalid. In other words, if it is believed that an arbitral award is attached to the seat's legal system, then its annulment by a national court would mean that it no longer exists.

The Convention, by giving discretion to states to enforce an annulled arbitral award, suggests that the validation of an international arbitration should be sought elsewhere, and not in a member state's legal system. One can infer that, from the beginning, contracting states were aware of the fact that international commercial arbitration does not stem from a nation-state's legal system. Otherwise, if the validity of an award originated from a national legal system, then invalidation of that award by that jurisdiction would leave no grounds for other states to recognize and enforce the award.

Some French courts have conceived of the transnational nature of international commercial arbitration. They similarly have acknowledged that annulment of an arbitral award does not affect the existence of the award because it does not belong to any jurisdiction. Therefore, they enforce the award

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[50] There are also opposite opinions about the possibility of enforcement of an annulled arbitral award. The grounds of arguments vary. Some of them argue that the arbitral award is part of the seat's legal system and it does not exist after being annulled by the court of the seat. Others bring up the notion of comity and mutual respect as an obstacle to recognize other jurisdictions' decisions. See Robert Bird, "Enforcement of annulled arbitration awards: a company perspective and an evaluation of a 'new' New York Convention" (2012) 37:4 North Carolina journal of international law and commercial regulation 1012; see also Matthew D Slater, "On annulled arbitral awards and the death of Chromalloy" (2009) 25:2 Arb lnt'l 271; see also Joseph E Neuhaus, "Current Issues in the Enforcement of International Arbitration Awards" (2004) 36:1 The University of Miami inter-American law review 23.

regardless of its having been annulled by the court of its seat. Among the law cases, Hilmarton[51] and Putrabali[52] have drawn special attention.

In the Hilmarton case, the French Supreme Court decided to enforce an ICC award that had been annulled by a Swiss court, on the basis that international arbitration awards are not integrated within the seat's legal system. The court ruled that: "… the award rendered in Switzerland is an international award which is not integrated in the legal system of that state, so that it remains in existence even if set aside and its recognition in France is not contrary to international public policy."[53] Now the question is: if an arbitral award does not belong to a nation-state's legal system, where does it originate?

In the Putrabali case, the court stated that: "An international arbitral award, which is not anchored in any national legal order, is a decision of international justice whose validity must be ascertained with regard to the rules applicable in the country where its recognition and enforcement are sought.…"[54]

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[51] Cass civ 1re, 2 March 1994, (1995) Société Hilmarton Ltd v Société Omnium de traitement et de valorisation (OTV) Bull civ 1 79, No 104; Albert Jan van den Berg, *Yearbook Commercial Arbitration 1995*, vol. XX (The Hague Kluwer Law International, 1995) at 663-665.

[52] Cass civ 1er, 29 June 2007, (2007) PT Putrabali Adyamulia v. Rena Holdinget, Bull civ 1 No 250; Emmanuel Gaillard, "Note - 29 juin 2007 - Cour de cassation (1re Ch. civ.)"(2007) 2007:3 Revue de l'Arbitrage 517.

[53] [Translation adopted from] van den Berg, at 663-665.

[54][Translation adopted from] Albert Jan van den Berg, *Yearbook Commercial Arbitration*, vol. XXXII (The Hague: Kluwer Law International, 2007) at 299-302. Original language: "Mais attendu que la sentence internationale, qui n'est rattachée à aucun ordre juridique étatique, est une décision de justice internationale dont la régularité est examinée au regard des règles applicables dans le pays où sa reconnaissance et son exécution sont demandées ; qu'en application de l'article VII de la Convention de New-York du 10 janvier 1958, la société Rena Holding était recevable à présenter en France la sentence rendue à Londres le 10 avril 2001 conformément à la convention d'arbitrage et au règlement de l'IGPA, et fondée à se prévaloir des dispositions du droit français de

The French Supreme Court mentioned international justice as a source of international arbitration. It referred to a transnational legal order vis-à-vis national legal systems by way of "international justice."

It seems that the word "may" in the phrase "Recognition and enforcement of the award may be refused" in Article V of the New York Convention signals a very important aspect of international arbitration. It demonstrates that arbitration awards are not part of any state's legal system and the validation of arbitral awards should be understood in another context. The French Supreme Court suggests international justice as a source. The term "international justice" may be construed in different ways. For Emanuel Gaillard, in an article published in the *New York Law Journal* a few months after the issuance of the court's decision, the phrase refers to "the community of all states." According to his interpretation, the court's decision about recognition or annulment of the award "has no impact on the objective existence of the award as an *autonomous international decision* which derives its legal force from *the community of all states* and not from a single legal system."[55] One may also raise the notion of a self-validating arbitral legal system and describe a state's refusal to recognize an annulled award as the result of a relationship between two independent legal systems. It is a matter for the legal systems' internal regulations to determine how they interact with each other.

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l'arbitrage international, qui ne prévoit pas l'annulation de la sentence dans son pays d'origine comme cause de refus de reconnaissance et d'exécution de la sentence rendue à l'étranger."

[55] Gaillard, "The Representations" *supra* note 14. [Emphasis added]

B. Limitation of states' intervention

Limitation of states' intervention in international commercial arbitration can be discussed in two different stages. The first stage relates to the emergence of new terms and notions that force national legal systems to broaden their vision while dealing with international commercial arbitration. The second stage is when the international arbitration acts prevent states from intervening in the arbitration process. In this part, I highlight these two stages as new movements that signal the existence of an autonomous arbitral legal system.

1. Advent of new terminology in international commercial arbitration (Notion of transnational public policy)

The tendency to acknowledge the independence of an arbitral legal system can be conceived through the creation of new judicial opinions and the emergence of a new terminology in the international arbitration community.

The notion of public policy in international commercial arbitration is a good example that demonstrates how national legal systems have created the concept of a "truly international public policy" or transnational public policy in response to transnational arbitration. The terms "international public policy" and "truly international public policy" are used in different contexts. The former is a public policy that national courts apply in international arbitration cases, and its domain is narrower than the public policy in domestic arbitration cases. "Transnational public policy" is a newly developed term that refers to "fundamental rules of natural law, principles of universal justice, *jus cogens* in

public international law, and the general principles of morality accepted by what are referred to as "civilized nations."[56] Transnational public policy has been recognized by some jurisdictions, and several courts have addressed it. For instance, the Paris Court of Appeal referred to the concept of "truly international and universally applicable public policy."[57] In 1994, the Swiss Federal Supreme Court in the famous Westland case again cited the notion of transnational public policy and also tried to give a definition different from the traditional meaning that had been adopted by national courts. The court defined "universal public policy" as "fundamental principles of law that are to be complied with irrespective of the connections between the disputes and a given country."[58]

That would be a rational response to readjust the interpretation of old concepts according to new developments. When they were confronted with modern international commercial arbitration and acknowledged a relative independence of its source from national legal systems, these national legal systems tried to provide a new interpretation of public policy. Consequently, they differentiated the domain of public policy when it is applied in international commercial arbitration.

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[56] Audley Sheppard, "Public Policy and the Enforcement of Arbitral Awards: Should There Be a Global Standard?"(2004) 1:1, transnational dispute management 1 at 3; see also Mark Buchanan, "Public policy and international commercial arbitration"(1988) 26:3 Am Bus LJ 511 at 3.

[57] CA Paris September 30, 1993, European Gas Turbines vs Western International Ltd (1994) rev. arb. 359; cited in and translated by Gaillard, *Legal Theory supra* note 8 at 60. (Original text: "d'essence véritablement internationale et d'application universelle.")

[58] Swiss Federal Supreme Court, April 19, 1994, Westland Helicopters Ltd., ATF 120 II 155; cited in and translated by ibid. (Original text: "les principes fondamentaux du droit qui s'imposent sans égard aux liens du litige avec un pays déterminé.")

2. The harmonization and modernization of national legislations

As a response to the growth and development of international arbitration, many states started to harmonize their arbitration laws. Adoption of the UNCITRAL Model Law (UNCITRAL Model Law on International Commercial Arbitration)[59] in the mid 1980s further helped the adaptation of arbitration acts to the reality of modern international arbitration.

According to the preamble of the "Model Law," its main purpose is to establish "… a unified legal framework for the fair and efficient settlement of disputes arising in international commercial relations."[60] What the Model Law is seeking to achieve is to encourage states to adopt a uniform set of arbitration rules that have emerged from the real practice of arbitration. This uniform set of rules in the preamble in its revised version is meant to reflect the general principles of arbitration that are fostered by arbitration users.[61]

The experience of the Model Law proves the important role of private actors in global governance, for arbitration users have been making global law. The model Law is not based on states' legislation; it is a set of general rules extracted from arbitration practice and copied by states.

The Model Law experience teaches us that in order to modernize arbitration rules the appropriate approach is to grant legislative power to the

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[59] Hereinafter "Model Law". United Nations document Al40117, annex I; as adopted by the United Nations Commission on International Trade Law on 21 June 1985, online: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html.

[60] Ibid.

[61] Ibid. The Model Law recognizes "the need for provisions in the Model Law to conform to current practices in international trade."

community that knows best the needs and the reality of arbitration. Some states have realized that to modernize arbitration rules and to create a legal foundation that is more consistent with the needs of international arbitration users is to recognize a certain kind of autonomy for international arbitration. Therefore, the modernization of national legislation has developed in a new direction to take a more flexible approach and respect the greater autonomy of arbitral processes further than what the Model Law suggested.

The new developments in legislation and judicial opinion show that states further tend to consider international commercial arbitration as an efficient autonomous legal system. One may argue that states' liberal approach towards the arbitral process could be the result of competition among states in order to attract more international arbitration as a growing market.[62] Economic purposes may play a role for those states that have taken such an approach; but more importantly, this move demonstrates states' tendency to recognize relative independence of international commercial arbitration.

Here I would like to discuss some examples of the legislative shifts towards international arbitration in different jurisdictions. The first shift is "the elimination of mandatory judicial review."[63] According to this rule, a state does not intervene in international arbitration processes when there is no specific connection between the state and the arbitration case, for instance when neither party is a citizen of that state nor has other connections with the place of contract

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[62] Hanotiau, *supra* note 49 at 92.

[63] Hossein Abedian, "Judicial Review of Arbitral Awards in International Arbitration-Acase for an efficient System of Judicial Review" (2011) 28:6 J Int'l Arb 553 at 562.

or performance. This principle was initially introduced by the French court of appeal in the "Gotaverken" case, where the French court did not find any grounds to rule on the case according to French arbitration law becomes it "[is] in no way anchored in the French legal system as both parties are foreign and the contract was concluded and was to be performed abroad." The court also formed that the parties' choice of seats is usually based on the neutrality of that jurisdiction towards international arbitration. It provided that the "location where arbitral proceedings take place, which is chosen exclusively to ensure neutrality, was not significant and could not be considered to be an implicit manifestation of the parties' will to subject themselves, even on a subsidiary basis, to French procedural law."[64] Probably, the French court inspired Belgium when the latter adopted a *laissez-faire* approach dealing with international arbitral awards. Article 1717 (4) of Belgium's international arbitration act of 1985 provides that "The Belgian Court can take cognizance of an application to set aside only if at least one of the parties to the dispute is either a physical person having Belgian nationality or residing in Belgium, or a legal person formed in Belgium or having a branch (*une succursale*) or some seat of operation (*un siège quelconque d'opération*) there."[65]

The second example relates to those states that respect the parties' agreement to give up the procedure for annulment of arbitral awards. Some states replaced mandatory state intervention by allowing parties to waive the right of

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[64] Gaillard, *Legal Theory sura* note 8 at 63-64.

[65] I should mention that article1717 (4) was changed in 1998. See the Law of 19 May 1998 Amending the Belgian Legislation Relating to Arbitration, online: <http://www.jus.uio.no/lm/belgium.code.judicature.1998/portrait.pdf>.

action for annulment against arbitral awards. For instance, Article 192 of the Swiss Private International Law Statute provides that "If none of the parties have their domicile, their habitual residence, or a business establishment in Switzerland, they may, by an express statement in the arbitration agreement or by a subsequent written agreement, waive fully the action for annulment or they may limit it to one or several of the grounds listed in Art. 190(2)."[66]

Belgium, too, adopted new law in 1998 and replaced section 4 of Article 1717 with the following paragraph: "The parties may, by an express statement in the arbitration agreement or by a subsequent agreement, exclude any application to set aside the arbitral award where none of the parties is either an individual of Belgian nationality or residing in Belgium, or a legal person having its head office or a branch there."[67] In a recent modification of its arbitration law, France has also adopted the same rules. Article 1522 of French Code of Civil Procedure as amended in 2011 provides that "By way of a specific agreement the parties may, at any time, expressly waive their right to bring an action to set aside."[68] The implication of both the mandatory and voluntary elimination of judicial review is that states are tending to recognize that the validity of international arbitration

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[66] Article 192 (1) and (2) of the Swiss Federal Statute on Private International Law, Chapter 12 of the Private International Law Act 1987, online: <https://www.swissarbitration.org/sa/download/IPRG_english.pdf>.

[67] The Law of 19 May 1998 Amending the Belgian Legislation Relating to Arbitration, online: <http://www.jus.uio.no/lm/belgium.code.judicature.1998/portrait.pdf>.

[68] Nouveau Code de procédure civile art 1522 NC proc civ, online: http://www.legifrance.gouv.fr/jopdf/common/jo_pdf.jsp?numJO=0&dateJO=20110114&numTexte=9&pageDebut=00777&pageFin=00781.; Translation adopted from the website of International Arbitration Institute online: <http://www.iaiparis.com/pdf/FRENCH_LAW_ON_ARBITRATION.pdf.> (Original text: "Par convention spéciale, les parties peuvent à tout moment renoncer expressément au recours en annulation.")

does not derive from states' legal systems. Professor Gaillard has described this clearly, and he concludes, "[n]ational legal orders are thus gradually abandoning the idea that the source of validity of arbitral awards necessarily lies in the legal order of the seat, conceived as a forum, or even in any national legal order, and [are] moving towards the conception that recognizes the existence of an arbitral legal order."[69]

C. Use of a non-state body of law in practice

The last sign of the existence of an arbitral legal system that I would like to mention is the possibility of replacing a national law as proper law by "rules of law" in the practice of international commercial arbitration.[70] Qualitatively and quantitatively growing so-called "soft" laws in international business (including codified legal principles, guidelines, model contracts, standard terms, and model laws),[71] increasing the number of referrals to trade usages and customs in international contracts, and some scholars advocating the new notion of a *lex mercatoria*[72] have given a new dimension to the emergence of non-state

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[69] Gaillard, *Legal Theory sura* note 8 at 66. One can argue that arbitration users want the seat and the judicial oversight of the seat. Therefore, Belgium's retreat resulted from the fear of becoming an unfavorable place for the international arbitration by total elimination of the setting aside procedure.

[70] Marie-Laure Djelic, "From the Rule of Law to the Law of Rules" (2011) 41:1 International Studies of Management & Organization 35.

[71] José Angelo Estrella Faria, "Future Directions of Legal Harmonisation and Law Reform : Stormy Seas or Prosperous Voyage?" (2009) 1-2 Unif L Rev 5 at 7.

[72] See Philippe Fouchard *et al*, *Fouchard, Gaillard, Goldman on international commercial arbitration* (The Hague; Boston: Kluwer Law International, 1999) at 801; but see Thomas

substantive regulations. These phenomena have caused national laws to become more likely to be conceived as default laws. Furthermore, the design of many detailed procedural rules and guidelines has made commercial arbitration independent of national regulations and forced the latter to be more flexible and permissive to adjustments based on party autonomy.[73]

In international commercial arbitration cases, there is no doubt that it is the tribunals' duty to take into account general principles, trade usages, standards terms, commercial norms, and even relevant market expectations for deciding a case. In this regard, Professor Bernard Hanotiau states:

> [T]hese practices and trade usages, and general principles of commercial arbitration, have found their way into the decisional process of international commercial disputes; either through the application of international conventions such as the Vienna Convention on the Sale of Goods or the UNIDROIT Principles when they are applicable; or because they are part of the national law applicable to the dispute; or because their existence has been progressively ascertained by court decisions and arbitral awards.[74]

He claims that general principles and trade usage suffice to resolve most commercial disputes without any need to refer to a national law.[75]

Schultz, "Some Critical Comments on the Juridicity of Lex Mercatoria"(2008) 10 Yearbook of Private International Law 667.["Lex Mercatoria"]

[73] Rau, *supra* note 36.

[74] Hanotiau, *supra* note 49 at 98.

[75] Ibid at 97.

Today, many modern statutes and institutional arbitration rules permit parties and arbitrators to choose transnational rules to govern the resolution of a dispute. Article 1511 of the new French code of civil procedure provides that "The arbitral tribunal shall decide the dispute in accordance with *the rules of law* chosen by the parties or, where no such choice has been made, in accordance with *the rules of law* it considers appropriate. In either case, the arbitral tribunal shall take *trade usages* into account."[76] Among arbitration institutes, the International Chamber of Commerce has also allowed parties and arbitrators to choose rules of law. According Article 21 of the ICC rules, "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."[77] This article also urges the arbitral tribunal to take into account relevant trade usages. Even some conservative arbitration rules like UNCITRAL (United Nations Commission in International Trade Law) have allowed the application of "rules of law" in cases when the parties have so chosen. Therefore, in the absence of parties' choice, an arbitral

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[76] Translation adopted from the website of International Arbitration Institute online at http://www.iaiparis.com/pdf/FRENCH_LAW_ON_ARBITRATION.pdf; original language: «Art. 1511. Le tribunal arbitral tranche le litige conformément aux règles de droit que les parties ont choisies ou, à défaut, conformément à celles qu'il estime appropriées. Il tient compte, dans tous les cas, des usages du commerce », online :<http://www.legifrance.gouv.fr/jopdf/common/jo_pdf.jsp?numJO=0&dateJO=20110114&numTexte=9&pageDebut=00777&pageFin=00781>.

[77] [Emphasis added]; 2012 ICC Arbitration Rules, online: http://www.iccwbo.org/products-and-services/arbitration-and-adr/arbitration/icc-rules-of-arbitration/#article_21.

tribunal, when there is a conflict of rules of law, has to choose a national law to govern the case. [78]

One could argue that statistics do not support the claim that "rules of law" are widely used by parties in international arbitration. By reviewing arbitration agreements and applicable laws as well as arbitration cases in recent decades, one does not observe an accretion of the use of these rules in practice; but two things should be borne in mind. First, most parties and their counsel are not well-informed about non-national rules. In a survey, it was revealed that the more familiar lawyers are with transnational rules the more willing they are to choose those rules as applicable law.[79] In addition, if there is reluctance, it is due to the parties' concerns about enforceability of the award. In other words, the uncertainties that parties have are related to states' recognition of choosing transnational rules as applicable law, not about the transnational rules themselves. More importantly, the survey revealed that transnational rules are not being used only as applicable law, they also have a very important role to play in the negotiation, contract drafting, and conflict-resolution processes.[80]

We live in an era of globalized arbitral procedure and highly harmonized substantive treatment of international commercial disputes.[81] Making law in

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[78] Article 35(1) of UNCITRAL arbitration Rules: "1. The arbitral tribunal shall apply *the rules of law* designated by the parties as applicable to the substance of the dispute. Failing such designation by the parties, the arbitral tribunal shall apply *the law* which it determines to be appropriate."

[79] Christopher R. Drahozal & Richard W. Naimark, *Towards a science of international arbitration: collected empirical research* (The Hague, The Netherlands: Kluwer Law International, 2005) at 221.

[80] Ibid at 224.

[81] Kaufmann-Kohler, "Globalization of Arbitral Procedure", *supra* note 4 at 1319.

international commercial arbitration is not a political fact; it is a "bottom-up lawmaking"process[82] in which the rules have emerged from real transnational and trans-systemic practices. The outcomes of cases and practices have shaped translational regulations as much as they have forced states to modernize and adopt their regulations according to them. Consequently, according to this sociology of law, the source of the international procedural and substantive laws that have been collected in transnational sets of rules and in national laws are interconnected. Therefore, referring to either one in arbitration agreements should not make any great difference.

4) Conclusion

Before engaging in a theoretical discussion about the existence of the international arbitral legal system, I discussed the most important consequences of globalization that have caused international arbitration to be transformed from a mere dispute-resolution mechanism to a self-validating legal system. I described the mutual interaction between law and the economy and how they force each other to evolve. I concluded that the globalized market has forced international commercial arbitration as the most desirable dispute-resolution mechanism to become an institutionalized and sophisticated self-organized legal system. It is also postulated that, as a result of globalization, the private sector, including individuals and entities relating to international commercial arbitration, has

[82] See Levit, supra note 33. (For more information about role of private transnational sector in shaping the law.)

gained more power in shaping the international order. The shift in power has caused changes in how we conceive "law" in the international context as well as providing an opportunity for international arbitration to act more autonomously. I also explained how the interaction between and among global arbitration communities has brought about a major evolution in the nature of international commercial arbitration. Systematic exchange of ideas, competition among members of the international arbitration community, the expectations of merchants, and the challenge of imbalances in North-South relationships have made international commercial arbitration subject to many necessary transformations. These contributing factors have also led it towards becoming a valid and credible legal system in order to better apply justice in the international commercial relations.

The transformation of international commercial arbitration to an independent legal system has broadly influenced practice. It has also found its way into international treaties, legislation, and court decisions. Although recognition of an autonomous arbitral legal system does not fully validate an arbitral legal system, it is considered a sign of the efficiency of a reliable system that supports the international business activities. I further discussed the possibility of enforcing annulled awards in the New York Convention, the limitation of states' intervention in arbitration processes, and the tendency towards a replacement of a national law by "rules of law" as the main signs affirming the validity of an arbitral legal system.

CHAPTER TWO
Theoretical Approach to an Arbitral Legal System (The Concept of "Law" in International Commercial Arbitration)

1) Introduction

The conceptualization of international commercial arbitration as an autonomous legal system has created theoretical discussions about the legality and systematicity of arbitration. In regard to legality, a series of discussions has been initiated about the capability of arbitral norms and customs to be considered law. In these discussions, scholars have assessed the legality of arbitral system by using various theories. They have attempted to determine the substantive and procedural qualities of "law" based on theories of law. Then, they have assessed the legality of the arbitral norms or customs according to these theories. With respect to systematicity, supporters and opponents of the arbitral legal system have tried to determine the essential elements of a legal "system" with emphasis on the meaning of system, in order to evaluate the systematicity of commercial arbitration.

At the first stage, when I asked the question "What is law?" I was, naturally, unsure where I would find the answer. I was not certain whether the question is a philosophical, political, or scientific one, and was diverted into

studying philosophical texts, social science research works, and legal theories' books. To solve this problem of focus, I gathered a long list of materials, any text that could presumably address this type of question. The result was overwhelming. I found an excessive number of resources ranging from books by ancient philosophers like Plato to those by recent ones like Hegel, writings from early anthropologists to the modern sociologists, and documents from pure legal positivists to modern pluralists. Philosophers from various schools, sociologists and anthropologists from different stripes, and national and international lawyers have attempted to determine what "law" is. Given that law has been conceptualized from different perspectives and in various disciplines, I found that its conceptualization, particularly in a transnational context, is one of the toughest tasks in the legal field.

In the second chapter, my objective is to show first, through historical analysis, how different social, economic, and political factors have shaped the concept of law in order to adjust the concept to be in line with the real practices. Second, by focusing on today's international legal system with respect to the emergence of transnational rules of law in the field of international commercial arbitration, I argue in favor of the necessity of a re-conceptualization of the notion of law according to the current circumstances.

In order to fulfill the objective, I will discuss, by historical analysis, various concepts of law in order to demonstrate the evolutionary nature of law and the impossibility of finding a comprehensive definition of law or a set of fixed substantive and procedural qualities that can be applied in any society. In addition, I will try to show that in each period political, economic, and social

shifts have caused transformations in the concept of law. Furthermore, I will discuss various theories of law that arbitrators have applied to theorize the arbitral legal system. Finally, I will attempt to choose the most appropriate theories that are compatible with the reality of international commercial arbitration.

2) Evolutionary course of the concept of law

Painting a clear picture of the concept of law is not a new field of study. Since the beginning of the human sciences, the determination of the concept of law has attracted different groups of scholars from various disciplines and with different approaches. Philosophers first raised the question of the meaning of the concept of law. Therefore, this early approach was essentially philosophical. It was a common tradition from early philosophers like Plato and Aristotle to the modern ones like Kant and Hegel to dedicate part of their theories to the definition of law. In the eighteenth and nineteenth centuries, the knowledge of law increasingly developed and became an independent discipline. The science of law became self-sufficient and jurists tended to distance their views from the philosophical approach and to adopt a jurisprudential approach. While the nature of the question altered to a jurisprudential one, the philosophical approach still had an influence on lawyers' insights.[83] Beginning in the mid-fifties of the twentieth century, due to the development of the social sciences and under the influence of growing technology, a new discipline with a new approach became

[83] Cairns Huntington, *Legal philosophy from Plato to Hegel* (London: Oxford University Press, 1949) at 2.

involved in the study of the concept of law. In this period, the social scientific concept of law was the main trend. In contrast to the jurisprudential approach, which puts the emphasis on sovereign states, the social scientific notion of law focuses on scientific methods of determining law in a society.

In order to construct a concept of law, international commercial arbitration theorists have been inspired by these three (philosophical, jurisprudential, and social scientific) approaches. Some theorists inspired by philosophical concepts tend to conceptualize law as natural and pre-existing rational rules and take a naturalistic approach. Others who are inspired by jurisprudential legal theories often adopt a positivist theory. The third group, with regard to the emergence of transnational rules and regulations, has given up the positivist idea and has tried to emancipate law from states' monopoly, thereby adopting the scientific approach.

In the following part, I am going to briefly investigate different approaches to the concept of law in general and in international arbitration in particular according to each approach. I am pursuing two main goals in this section. The first goal is to demonstrate that law is a dynamic phenomenon, and that in order to define it, one has to take into consideration all the circumstances and specific needs of a time. The second goal is to introduce different schools of thought about the notion of law in international arbitration in order to choose the most appropriate to the nature of international arbitration as an independent legal system.

A. The Philosophical Concept of Law

Philosophers were the first group to ask the question about the concept of law. Since the beginning of philosophy, there has been a steady tradition among philosophers to define the term "law". From ancient Greece to the nineteenth century, almost all the major thinkers expressed their visions about law and tried to theorize it according to their ideologies and schools of thought. In this period, the dominant concept of law was known as natural law theory. Natural law is an ontological theory. In other words, according to this theory, law is generally conceptualized as a "universal standard of legal norms and structure"[84] that has to be in conformity with a higher concept. According to natural law theory, law is a static phenomenon that never changes over the course of history. Therefore, changes in circumstances and the environment never allow deviation from its mandates.[85] Being "trans-historic" is one the fundamental characteristics of this theory. The principles of natural law have their roots in an abstract world and are not extracted from human experience. Therefore, laws, or at least the general principles, are not inspired by social, scientific, or cultural developments.[86]

Natural law theory has been attractive in different eras from the ancient Greeks and Romans to modern traditions such as Western legal theories and international legal traditions. The ontological focal point also varies in different schools of thoughts. The central point of a natural law theory could be, for

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[84] James T McHugh, *The essential concept of law* (New York: Peter Lang, 2002) at 12.

[85] Ibid.

[86] Ibid.

instance, the law of the nature, the notion of balance, or divine commandments. Whatever the focal point is, conformity with the central point is a fundamental requirement for legitimization of law.[87]

In the mainstream understanding of the natural law tradition, morality is the source of the validity of law. In other words, natural law is an intersection of law and morality. According to this interpretation natural law tries to resolve the tension between what "is" and what "ought to be".[88] John Finnis states: "a theory of natural law claims to be able to identify the conditions and principles of the right-mindedness, of good and proper order among persons, and in individual conduct."[89] In doing so, a naturalist studies the practices and analyzes them according to a general concept of morality to "distinguish the practically unreasonable rule from the practically reasonable one."[90]

The principles of natural law are considered the universal moral rules. According to the natural law, humans share a mutual aim and intellect; and they follow the same rules of conduct. Therefore, by means of this shared morality, mankind is able to distinguish a just behavior from an unjust one.

John Finnis sets out three sets of natural law principles that more or less correspond to the concept of modern natural law theory in international and transnational practices. The first principle is a set of basic practical precepts that are the result of the primitive forms of humans' striving to find out how to act.

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[87] Ibid.

[88] Raymond Wacks, *Philosophy of law, a very short introduction* (Oxford: Oxford University Press, 2006) at 10.

[89] John Finnis, *Natural law and natural rights* (Oxford: Oxford University Press, 1979) at 18.

[90] Ibid.

The second principle is a set of rules regarding "methodological requirements" to differentiate the reasonable and "morally right" act from unsound and morally fallacious practices. The last principle refers to "general moral standards."[91] According to these principles, it seems that natural law—at least as Finnis conceives it—seeks to rationalize ethics and morality in legal practice. In other words, in order to put the universal moral standards into daily practice, they should be translated into an efficient method.

In the modern age, natural law has played a significant role, especially in the events when it was necessary to find a universal source of normative order that all human society could rely on. The principles of human rights, for instance, are those universal ethical rules that have been established on the basis of natural law theory. Humanitarian law and relative international legal orders are shaped fundamentally by naturalism. In particular, the Nuremberg Tribunal, which was responsible for the prosecution of war crimes after World War II, recognized the requirement for a "higher law to exist within 'universal' principles of human dignity that not only forbade these sorts of crimes but also required officials, within reasonable bounds, to resist and, if possible, prevent them from happening."[92]

The transnational and universal principles of international commercial arbitration have inspired some scholars to adopt natural law theory to explain the arbitral legal system. René David and Bruno Oppetit are known as scholars who

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[91] Ibid at 23.

[92] Wacks, *supra* note 88 at 10.

have taken a juranaturalistic approach.[93]

René David has explicitly stated that the anational rules that have been developed by the arbitrators are based on universal natural law. He adds that the new commercial law is an a-national legal order that completely detaches itself from strict and codified national legal systems. According to him, arbitrators go beyond the strict laws to find the best solution regarding the parties' special interests. In other words, the application of "amiable composition" and fairness are two aspects influenced by natural law theory. David states that:

> The new commercial law, as developed by corporatist arbitral tribunals, is strongly influenced by natural law. Like natural law and ancient commercial law, and despite national codifications, this new commercial law is international in nature. As such, it moves away and distinguishes itself from positive national law. Moreover, contrary to 'positive' law in various countries, it is characterized by arbitrators' desire to take into account the commercial interests of the parties, even if that entails sacrificing, if need be, their strict rights. It is just as important to maintain good relations as it is to obtain what is owed to one in a given dispute.[94]

Arbitrators rely on the existing superior moral principles to settle international arbitration cases. In fact, they refer to principles of fairness, and to amiable composition, instead of referring to a national law. They have obtained this right from the parties who agreed to resolve their conflicts in a flexible and

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[93] Gaillard, *Legal Theory sura* note 8 at 41.

[94] René David, "Droit natural et arbitrage", *Essays to Commemorate the Sixtieth Birthday of Kotario Tanayo* (Tokyo: Yhikaku, 1954) 19 at 24; [translated by] Gaillard, *Legal Theory sura* note 8 at 41-42.

broader framework different from that of national courts. Therefore, arbitrators as the legitimate agents of parties have the right to assess the validity of those moral principles.

Bruno Oppetit takes a slightly different approach to the transnational arbitral legal system. He argues that disintegration of the international rules is against the nature of the international commercial community. The fragmentations that exist within transnational laws and practices may contradict the nature and interests of the whole community. He adds that given that any fragmentation tends to become consolidated, the international arbitration community has created a universal concept of law, such as general principles and the *lex mercatoria*, to prevent contradictory regulations and practices. He also states that: "[international commercial law] for its part, clearly manifests a desire for unity and universality, based on the common needs and interests of the international economic community. As such, it does not accord with a fragmentation of the international legal framework and encourages the use of unifying legal notions, such as *lex mercatoria*, general principles of law, or truly international public policy."[95]

In addition to the role of the abovementioned arbitrators, the juranaturalistic approach can be observed in some arbitral cases and scholars' ideas without claiming that those rules constitute an independent legal system. The universal moral principles and standard ethical values play an important role in the arbitration process. They can be used for the purpose of interpretation,

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[95] Bruno Oppetit, *Philosophie du droit* (Paris: Dalloz, 1999) at 119, n. 104; cited by Gaillard, *Legal Theory sura* note 8 at 42.

filling in the gaps between laws, and completion of the governing laws when the chosen law is silent or incomplete. They may also override the chosen law when the application of that law contradicts the fundamental principle of the arbitration or infringes the universally accepted moral rules. Although these principles have never been considered as an independent legal system, on this view, such higher values exist and have to be respected by arbitrators even if they are not explicitly authorized to do so.

Professor Mayer has taken a naturalistic approach to the role of arbitrators. He has compared the duty of a domestic judge with that of an international arbitrator. He emphasizes the role of moral values in shaping legal rules and judicial orders. The orders that a judge or an arbitrator renders are based on moral principles. These principles can be extracted only by reasoning and cannot be found in the chosen applicable law or in any national law.[96]

Moral values are, therefore, those universal, superior, and natural laws that are conceptualized by arbitrators and applied to any case beyond the law chosen by particular parties. According to Professor Mayer, it is the arbitrators' responsibility to consider and adjust them in any national or international arbitral case. He states: "…an arbitrator has his own conception of his responsibility, his own moral standards, and they may lead him to consider as part of his mission other considerations, e.g. considerations related to public interest."[97]

Similarly, the natural law approach has been used by some arbitrators to

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[96] Pierre Mayer, "Reflections on the International Arbitrator's Duty to Apply the Law: The 2000 Freshfields Lecture" (2001) 17:3 Arb lnt'l 235 at 236.

[97] Ibid at 241; see also Gaillard, *Legal Theory sura* note 8 at 43-45.

answer the question of the origin of legality of the *lex mercatoria* as a set of rules. For instance, Professor Carbonneau has argued that the *lex mercatoria* incorporates natural law principles that are "part of the bargain in international contracts."[98] According to this idea, the *lex mercatoria* is deemed to be a set of rules superior to national or other chosen laws. It governs international commercial cases notwithstanding time, place, or context.

Regarding the legitimacy of such a set of rules based on the natural law approach, Thomas Schultz elaborates that: "the only determinant criterion of juridicity is the legitimacy of a rule, that is its moral value or conformity with some higher moral order."[99] Schultz, however, criticizes the natural law approach from three points of view. According to him, international commercial rules are practical rules necessary for the operation of international commerce; therefore, they do not bear a moral value.[100] In addition, it would be extremely controversial to determine whether a rule is moral or immoral. He questions the necessity of the conformity of a rule to higher moral values in order for it to be considered a "law" because, according to him, there exist laws that are morally wrong but are perfectly legitimate and applicable.[101]

The *jus naturale* concept of law has not attracted many advocates in the field of international arbitration; and the natural law theory has not thrived owing

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[98] Thomas Carbonneau, *Lex mercatoria and arbitration, a discussion of the new law merchant*, revised ed (New York: Juris Publishing, 1998) at 16; Schultz, *Supra* note 72 at 683.

[99] Ibid.

[100] Ibid.

[101] Ibid.

to the following facts: first, the naturalistic approach seriously undermines legal certainty; and second, by no means can one assess the credibility of the law, but one can only claim that it is self-evident. There are some defects in natural law theory that have an adverse impact on legal certainty in international arbitration. The question is whether general moral standards are really general? Finnis argues: "human beings are not all equally devoted to the pursuit of knowledge or justice, and are far from united in their conception of what constitutes worthwhile knowledge or a demand of justice."[102] Even if we think that there exist general moral principles, this does not mean that these principles are interpreted in the same way in all legal traditions. Moreover, moral principles are the result of a delicate process through which human individuals strive to find out how to act. Many people would argue that moral questions are purely personal matters; therefore, generalizing personal experience to a general principle would seem to be logically incorrect.

As I argued before, one may not find any way to assess the credibility of morally right acts and moral principles other than by reference to arbitrators' consciences, knowing that natural rules are discoverable only by natural means. One may argue that the credibility of a moral principle is self-evident and does not need to be proved. The answer is that perception of a moral principle is an individual experience that may differ from person to person. It seems that individualizing the perception of justice puts the reliability and legitimacy of law at risk.

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[102] Finnis, *supra* note 89 at 29.

B. The Jurisprudential Concept of Law

Since the early nineteenth century, philosophers have paid less attention to the concept of law; and therefore, the era of the jusnaturalistic approach to the concept of law seems to have come to an end. Professor Huntington Cairns gives two grounds why theorizing the concept of law was no longer the main focus of philosophers' work. He remarks that indeed, due to scientific developments and growth of technology, the main focus of philosophers was to theorize science and knowledge. In addition, law practice had become a detailed and technical practice. Law practitioners dominated the field of law and developed it in a direction that distanced legal science from philosophy.[103]

As the result of the gradual decline of the *jus naturale* approach, it was necessary to establish a modern theory of law that corresponds to the realities of the modern world. Some factors definitely influenced the establishment of the modern theory of law. First of all, specific socio-political changes, particularly modernism and liberalism, contributed to this alteration. Liberalism brought individuals' free will and subjectivity into the law-making process. Modernism, on the other hand, redefined the relationship between individuals' rights and sovereignty. As a result, "law" became the product of sovereign political institutions like parliament or the courts that posit the social norms or the will of the majority of society in official practices.

Modernism and liberalism also accompanied major economic changes and

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[103] Huntington, *supra* note 83 at 1.

caused lateral entities like law firms to emerge. The liberal economy and capitalism in the mid nineteenth century caused the sudden growth of legal practices and expansion of legal institutions. The field of law further advanced and became an independent field of learning with many specialized branches. Law distanced itself from the influence of other disciplines like philosophy and developed its own rules, principles, and concepts. Consequently, the "law" became jurisprudential and the product of legal and political practices.

The dominant modern concept of law is generally considered to be legal positivism. Legal positivism quickly became the dominant theory of law and has shaped the legal systems in almost all modern states. It is believed that positivism and modernism have a close relationship and that they have been progressing simultaneously.[104] As can be seen in today's world's legal systems, those states that want to be modernized have to revise their legal system and adopt legal positivism relative to their legal system's specifications.

1. Legal Positivism: Definition and Evolution

The geographical diversity and temporal differences of the adoption of legal positivism has made it difficult to define. Diverse modern legal systems from different continents have adopted legal positivism and have altered it according to their needs and specifications. Positivism in civil law states, for instance in France, is interpreted differently from that in common law states like

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[104] Marett Leiboff & Mark Thomas, *Legal theories, context and practices* (Sydney: Lawbook,Thomson Reuters, 2009) at 255.

England and the United States. Legal positivism has also experienced different transformations through its development. Considering geographical and temporal factors as well as the diversity of schools of thought, it is not an easy task to find an answer to the question of what legal positivism is. However, there are generally accepted features that distinguish positivism from other theories.

The fundamental point of positivist theory is that the only reliable source of law is pure logical and scientific experiment.[105] The origins of law are humans themselves and their social interactions. Unlike the naturalist, a positivist separates law from morality and other value-based sources of law.[106] Positivism is to conceptualize law as "what it is" instead of "what it ought to be." In order to promote legal certainty, legal positivism prefers not to refer to a universal, intangible, and undeterminable source of law. Therefore, in positivism, the legal framework is a definite one and law is analytical and descriptive rather than natural or supernatural.[107] The validity of a law is normally assessed according to certain characteristics and criteria.[108]

Raymond Wacks lists six major shifts that legal positivism experienced during its period of development from old and contemporary positivism to postmodern (pluralist) positivism.[109] Studying some of these six variations of positivism can help us to understand better the recent discussions among the positivist arbitrators who are analyzing the concept of law in the transnational

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[105] Wacks, *supra* note 88 at 57.

[106] Ibid at 32.

[107] Ibid.

[108] Leiboff & Thomas, *supra* note 104 at 255.

[109] Wacks, *supra* note 88 at 32-33.

arbitral legal system.

(a) Traditional Legal Positivism

(i) Formalism and Individualism

The first focal points of positivism are formal justice and individualism. Formalism basically means that humans require to be treated equally, and individualism demands that individuals are rewarded and punished based on what they deserve. Professor Hart clearly points this out in stating:

> There is therefore a certain complexity in the structure of the idea of justice. We may say that it consists of two parts: a uniform or constant feature, summarized in the concept "Treat like cases alike" and a shifting or varying criterion used in determining when, for any given purpose, cases are alike or different.[110]

(ii) Consequentialist and Utilitarian notions of justice

The start of positivism coincides with early capitalism. Therefore, the notion of law and justice was inspired by nineteenth-century capitalist ideas. One result of the commercial ideology of the period is the consequentialist analysis of law and justice. Jeremy Bentham's utilitarian approach to justice[111] and the economic

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[110] HLA Hart, *The concept of law*, 2nd ed (Oxford: Oxford University Press, 1997) at 156.

[111] See JJC Smart & Bernard Williams, *Utilitarianism, for and against* (Cambridge: Cambridge University Press, 1973).

analysis of law by some authors[112] brought new insights to legal positivism and affected the modern transnational concept of justice.

(b) Modern and Postmodern Legal Positivism

(i) Sovereignty and Law:

The legal positivist marks a new stage by reviving arguments about the validity of law from different angles. One of the most controversial arguments about the validity of law is sovereignty. The relationship between law and power is considered a key factor of the validity of law. According to John Austin, who developed his theory of law based on the notion of "command," it is a crucial characteristic of a valid "command" that its source is identified as a "political superior."[113]

(ii) Normative orders and efficacy

Hans Kelsen is the other positivist who has contributed greatly to the advancement of legal positivism. Kelsen's theory concerns human norms as constructing the elements of a legal system. He states: "A norm, in order to be valid or binding must be authorized by another norm which, in turn, is authorized

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[112] See Wacks, *supra* note 88 at 217.

[113] Ibid at 72; See WL Morison, *John Austin* (Stanford, Calif.: Stanford University Press, 1982); see also John Austin & Wilfrid E Rumble, *The province of jurisprudence determined* (Cambridge: Cambridge University Press, 1995).

by a higher norm in the system."[114] And "the hierarchy of legal norms that form a legal system is ultimately traced back to the *Grundnorm* or basic norm of the legal system."[115] Therefore, according to Kelsen, a legal system consists of complex and multi-layered norms in which each norm gains its validity from a higher one and the highest norm gets its validity from the basic norm. According to Kelsen's theory, validity and efficacy have a close relationship: "It cannot be maintained that, legally, men have to behave in conformity with a certain norm, if the total legal order, of which that norm is an integral part, has lost its efficacy. The principle of legitimacy is restricted by the principle of effectiveness."[116]

(iii) Primary and secondary rules of law

The most influential figure in modern legal positivism is H.L.A. Hart. Professor Hart in his famous book *The Concept of Law* published in 1961 expressed his views about the concept of law and the basic requirements of a legal system. According to him, "social rules" are the basic element of the law. He differentiates law and non-legal entities by a set of common characters he calls "the internal aspect of rules."[117] This "internal aspect of rules" is not based on the mere "feelings" of individuals; rather, it is based on "externally observable physical behaviour" like "social criticism" or "pressure for conformity" that is

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[114] Wacks, *supra* note 88 at 90.

[115] Ibid at 91.

[116] Hans Kelsen, *General theory of law and state* (New York: Russell & Russell, 1961) at 119; Wacks, *supra* note 88 at 97.

[117] Hart, *supra* note 110 at 54-56.

"generally accepted by a social group."[118] For Hart, however, the rules of behavior are not sufficient to constitute a legal system. A legal system needs a set of secondary rules to provide systematicity. He states:

> There are therefore two minimum conditions necessary and sufficient for the existence of a legal system. On the one hand those rules of behaviour which are valid according to the system's ultimate criteria of validity must be generally obeyed, and, on the other hand, its rules of recognition specifying the criteria of legal validity and its rules of change and adjudication must be effectively accepted as common public standards of official behaviour by its officials.[119]

(iv) "Internal Morality of law"

As was discussed before, separation of law and morality is one of the main characteristics of positivism. But some positivist scholars have observed a necessary connection between law and morality. Among them, Professor Fuller has conceptualized his theory on "a procedural natural law" method.[120]

Unlike the classical naturalist who believed in the existence of a higher law, Fuller demonstrates that law has "internal morality," which means that the main objective of a legal system is to conform to the standard procedural principles, regardless of their substance. He lists eight failures in making rules; and then he concludes that in order to establish a legal system, one has to

[118] Ibid at 56.

[119] Ibid at 113.

[120] Wacks, *supra* note 88 at 33.

overcome these failures.[121] The eight principles he introduces as eight "desiderata" or "eight kinds of legal excellence towards which a system of rules may strive" are: Generality, Promulgation, Non-retroactivity, Clarity, Non-contradiction, Possibility of compliance, Constancy, and Congruence between declared rules and official action.[122]

(v) Legal Pluralism

The anthropological approach to the concept of law challenges the validity of traditional and modern positivism from the social science point of view. Generally speaking, according to the characteristics of positivism, "law" is a set of hierarchical norms or commands posited by a sovereign state. In other words, in the most favorable form, a democratic state extracts rules out of the norms and behaviors of the majority of its society. The extracted rules are normally generalized and every member of the society is deemed committed to comply with the law. John Griffiths has called traditional and modern positivism a "centralist conception" and he describes it in the following way:

> In the legal centralist conception, law is an exclusive, systematic and unified hierarchical ordering of normative propositions, which can be looked at either from the top downwards as depending from a sovereign command or from the bottom upwards as deriving their validity from ever more general layers of norms until one reaches some ultimate norm(s). In

[121] Ibid; Lon L Fuller, *The morality of law* (New Haven: Yale University Press, 1964) at 39.

[122] Ibid; Wacks, *supra* note 88 at 34.

> either case, while the various subordinate norms which constitute "law" carry moral authority because of their position in the hierarchy, the apex itself—the sovereign or the Grundnorm or the rule of recognition—is essentially a given. It is the factual power of the state which is the keystone of an otherwise normative system, which affords the empirical condition for the actual existence of "law". Hence the necessary connection between the conception of law as a single, unified and exclusive hierarchical normative ordering and the conception of the state as the fundamental unit of political organization.[123]

"Legal centralism" is supposed to create a serious barrier for a society that ignores minorities' customary laws or the sub-legal system(s) that may co-exist in a society.[124] Therefore, legal pluralism has emerged to improve the shortcomings of positivism.

Legal pluralism has been interpreted in various ways. For example, from the anthropologist's point of view, pluralism is a way to recognize the customary law of communities in diversified societies. As Hooker puts it, pluralism is the coexistence of "multiple systems of legal obligation ... within the confines of the state."[125] His definition can be interpreted as recognition of customary law with an emphasis on the supremacy of the state law.[126] Legal pluralism from the juridical

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[123] [Citations eliminated] John Griffiths, "What is legal pluralism?"(1986) Journal of legal pluralism and unofficial law 1 at 3.

[124] Wacks, *supra* note 88 at 207.

[125] MB Hooker, *Legal pluralism, an introduction to colonial and neo-colonial laws* (Oxford: Clarendon Press, 1975) at 2.

[126] Griffiths, *supra* note 123 at 9.

point of view introduces customary rules as a source of law in multiple domestic and international commercial, political, and social institutions that interact and compete with states' laws.[127]

2. Transnational Positivist Approach to Arbitral Legal System

According to transnational positivism, non-state normative systems like the *lex mercatoria* and the *lex sportiva* become transnational systems of arbitral rules by being systematically referred to in international arbitration procedures. However, the legality of such a system relies on states' activities. The "states' normative activities" collectively are considered the main source of the arbitral legal system in the transnational positivist approach. The logic is clear: arbitration is a binding dispute-resolution mechanism only if it satisfies certain conditions that states generally have agreed on. In addition, arbitration will remain fruitless unless the ultimate result is recognized and enforced by a state.[128] According to this notion, the international arbitral system is considered "the convergence of all (national) laws."[129] In other words, not a particular state or states' regulations are the source of law; rather, national laws collectively create a transnational legal system. It is not necessary for a transnational legal principle to be confirmed by all states; it suffices that such a rule is generally accepted by civilized and modernized legal systems. According to the transnational positivist notion, law is

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[127] For more information see ibid at 11.

[128] Gaillard, *Legal Theory sura* note 8 at 46.

[129] Ibid.

a dynamic phenomenon; therefore, it evolves according to real situations and is interpreted differently by different states.[130] But in all cases, consensus among states is the best criterion to decide the credibility of a transnational principle.

Emanuel Gaillard, who revived the discussion in his famous article published in 2010,[131] emphasized the existence of the arbitral legal system. He initially, in a very philosophical manner, states that: "The arbitral legal order exists because it is perceived, because it is apprehended, often intuitively, but in a very real way by arbitrators, not necessarily by all the arbitrators, but by some arbitrators."[132] He also supports his idea by implementing the positivist approach. According to him, arbitral legal system is "… an idea, a mental representation of the role of the arbitrators and the source of their power to adjudicate."[133] In numerous cases, arbitrators have considered and implemented the concept of arbitral legal system in their daily practices without explicitly expressing it. Gaillard then articulates three grounds why arbitrators acquired such an approach. The grounds generally concern the practical aspects: first, the concept of international arbitration; second, particularity of the origin of the arbitrators' power to rule on a case; and third, arbitrators' role according to the operation of international commercial arbitration, which has made arbitration an attractive

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[130] Ibid at 50-51.

[131] Gaillard, "L'ordre juridique" *supra* note 14 at 891-892.

[132] Ibid at 893.[Translated by author] (Original text: "l'ordre juridique arbitral existe parce qu'il est perçu, parce qu'il est appréhendé, de manière souvent intuitive, mais très réelle par des arbitres, pas forcément par tous les arbitres, mais par des arbitres.")

[133] Ibid.[Translated by author] (Original text: "… une idée, une représentation mentale du rôle des arbitres et de la source de leur pouvoir de juger.")

dispute-settlement mechanism.[134]

It seems that Gaillard has adopted Kelsen's and Hart's notions of law to articulate his concept of arbitral legal system, especially when he tries to define a legal order and lists the fundamental characteristics of it. He states that due to the lack of a generally accepted definition of a legal order, one should consider the essential characteristics that constitute the legal order, which he defines as:

> A structured set of standards (norms) representing all degrees of imperativity and susceptible (likely) to respond to all matters relevant within the subject it purports to govern; capable of conceiving its sources; having subjects and bodies susceptible (likely) to ensure implementation of the standards (norms) it generates; and satisfying a minimum condition of effectiveness.[135]

Gaillard denies that transnational regulations that they are inconsistent and incomplete and have contradictory rules. According to him, the substantive transnational commercial rules are as binding, comprehensive, and structured as those of the domestic legal order. He believes that these allegations about incompleteness and contradictions are compensable by implementing general

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[134] Ibid.

[135] Ibid at 896.[Translated by author] (Original text: "* un ensemble structuré de normes revêtant tous les degrés d'impérativité et susceptibles de répondre A 1'ensemble des questions relevant de la matière qu'il prétend régir;

* capable de concevoir ses sources;

* possédant des sujets et des organes susceptibles d'assurer la mise en œuvre des normes qu'il génère ; et

* satisfaisant à une condition minimale d'effectivité").

principles such as good faith.[136] The general principles can be found in codified transnational principles like UNIDROIT (The International Institute for the Unification of Private Law), can logically be extracted from general principles, or by means of interpretation of rules, be obtained from the rules that reflect the minimum requirements of the international public order.[137]

In addition, the arbitral legal system has the capacity of reflecting its sources in a manner that differs from state positivism. Gaillard points out:

> It is the national legal systems collectively that legitimate its existence by accepting the arbitration phenomenon. The community of states has given international arbitration a genuine autonomy by accepting to entrust, to the parties who wanted it, the power of arbitrators to judge international commercial disputes and to recognize the result of the arbitral process— the arbitral awards— basically without scrutiny.[138]

He continues by observing that the arbitral legal system has its own subject and officials. Arbitrators as officials routinely extract norms from states' normative activities related to the operation of international business.[139] Gaillard also gives a statistical analysis to show how effective the arbitration process is. He claims that condemned parties execute 90 % of awards voluntarily without

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[136] Ibid at 897.

[137] Ibid at 897-898.

[138] Ibid at 898.[Translated by author] (Original text: "Pour ceux qui, comme 1'auteur de ces lignes, sont de stricts positivistes, c'est la convergence des ordres juridiques nationaux qui, par l'acceptation qu'elle manifeste du phénomène arbitral, en légitime l'existence. En acceptant de confier, pour les parties qui l'ont voulu, le pouvoir de juger les différends du commerce international aux arbitres et de reconnaître le produit du processus arbitral qu'est la sentence, sans la contrôler au fond, la communauté des États a conféré à l'arbitrage international une réelle autonomie.")

[139] Ibid at 898-899.

enforcement action in national courts.

The relationship between the arbitral legal system and other legal systems is a complex issue. In this regard, Gaillard briefly points out two related issues: namely, the recognition of the arbitral legal system by states' judicial systems and the conflicts of the arbitral legal system with international law. In regard to the former, a significant number of state legal systems have recognized it through diverse methods like confirmation of transnational public policy, authorization of parties to waive any action for annulment, and recognition of awards that have been annulled at the seat.[140] With respect to the latter, the situation is more complicated. International law and the arbitral legal system have a common territory, and there exists competition among them, particularly when it comes to protecting investment treaties. Some may question the usefulenss of elaborating a theoretical construction around the notion of the arbitral legal system if international law is designed to play the same role. In reply, Gaillard answers: "The acceptance of the hypothesis of the arbitral legal order does not detract from the reality and utility of international law. It simply provides a model on which can be built a structured representation of the settlement of disputes arising in the private or transnational relationships of the international community."[141]

Although the arbitral legal order theory was a gracious attempt to bring the

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[140] Ibid at 903-907.

[141] Ibid at 907. [Translated by author](Original text: "L'acceptation de l'hypothèse de l'ordre juridique arbitral n'enléve rien à la réalité et à l'utilité du droit international. Celui-ci fournit simplement un modéle sur lequel peut étre construite une représentation structurée du réglement des différends s'é1evant dans les relations privées ou transnationales de la communauté internationale.")

subject to the attention of the world's legal and business communities, it seems that the theory does have some internal contradictions and does not perfectly match with legal positivists' concept of law. It is not clear how the origin of arbitrators' power to rule in a case supports the idea of the existence of an arbitral legal system, especially when in most of cases the parties or their counsel are not aware of such a phenomenon. Therefore, it seems difficult to conclude that parties' consent to take part in arbitration is equal to their acceptance to have their disputes be governed by anational rules. This is even more obvious given the fact that the source of each arbitration case is different, and it is quite likely that parties' expectations are different as well. Another shortcoming of the theory is related to the positivist notion of law. The practical importance of the existence of the arbitral legal system does not suffice to conceive arbitration as a semi-independent legal system.

The publication of Gaillard's article initiated many discussions among scholars and arbitrators. Many of them criticized his theory of an arbitral legal system. These discussions began a series of debates about the basic elements of a legal system and especially about the concept of law in international arbitration. In particular, the legality and systematicity of the arbitral legal system has been analyzed on the basis of Hart's primary and secondary rules and Fuller's inner morality of law. In the following parts, I introduce them in detail.

(a) The Arbitral Legal System and Emerging Secondary Rules of Recognition

The international arbitration community has developed rules of conduct specific to itself. In order to distinguish right conduct from wrong, this small but very well-connected community generates social norms in various forms, such as rules, principles, doctrines, or other concepts. The members of the community also share common views about their conduct and function. They have a common understanding of their role as international adjudicators. They also conceive of themselves as being part of the international justice system. Through a more sophisticated process, their shared opinions take formal shape as codified arbitral rules and principles.

Kaufmann-Kohler calls this process the "globalization of arbitral procedure" and states that despite the differences in detail, arbitral principles are globally harmonized both in national and transnational sets of rules. She mentions that interactions among the members' of the international arbitration community coming from different legal systems and having various backgrounds have generated principles of transnational arbitral procedure in different forms, such as institutional arbitration rules, UNCITRAL arbitral rules, IBA rules on evidence, and so on.[142] Schultz also describes them as the "shared principled beliefs" that eventually bring forth "a global harmonization of the practice of arbitration." He states: "In the field of arbitration, these shared principled beliefs, relating to the most appropriate ways to deal with certain aspects of certain types of disputes,

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[142] Kaufmann-Kohler, "Globalization of Arbitral Procedure", *supra* note 4 at 1322.

have in part expressed themselves through a process that may broadly be characterized as codification, or in more jurisprudential terms 'formal positivization'. The[se] beliefs have [been] translated into formal amendments or creations of regulations_ model laws, institutional procedural rules and revisions of national arbitration laws. The result is a global harmonization of the practice of arbitration."[143]

Marmor, who conceptualizes law as a "social convention" connects it with Hart's secondary rules. He explains that Hart's secondary rules are basically a "social convention" among the officials who practice the law.[144] After a period of time and through practice, the social conventions turn into the binding customs that are thought of by members of a society as law.[145]

Marmor describes this process well when, in explaining the social thesis of legal positivism, he states:

> According to the social thesis, law is a social phenomenon, it is a social institution, and therefore, what the law is, is basically a matter of social facts. In every society there are certain social rules that determine what the law is, how it is to be identified, created and modified, and those social rules basically determine what the law in that society is.[146]

There are many examples of the social conventions that have been

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[143] Thomas Schultz, "Secondary Rules of Recognition and Relative Legality in Transnational Regimes" (2011) 56 Am J Juris 59 at 64.["Secondary Rules"]

[144] Andrei Marmor, "Legal Positivism: Still Descriptive and Morally Neutral" (2006) 26:4 Oxford J Legal Stud at 686; Schultz, "Secondary Rules" *Supra* note 143 at 63.

[145] Ibid at 63.

[146] Marmor, *supra* note 144 at 686; Schultz, "Secondary Rules" *Supra* note 143 at 63.

developing in the international arbitration community. But I would like to introduce two of them that have a close relationship with the systematization of the arbitral legal system. The first is the emancipatory tendency of international arbitration towards transnationalisation. For instance, it is a generally accepted practice to consider the transnational nature of arbitration. In the decision-making process, particularly, taking the transnational approach is crucial while interpreting a contract and an applicable national law as well as the application of public policy. In other words, to assess the credibility of the applicable national laws in arbitration, it is expected from an arbitrator to examine them under the *lex mercatoria*.[147]

The next example is the existence of an unwritten agreement in the international arbitration community to follow arbitral precedents. A survey has proved that in certain types of arbitration, such as sports arbitration and investment arbitration, the arbitrators have a tendency to cite previously decided arbitral cases. However, it has been argued that in international commercial arbitration it is neither widely practiced nor necessary to do so. This is not the idea I advocate; therefore, in the next part I will discuss the issue of precedent in commercial arbitration in more detail.[148] Generally speaking, it is a developed norm among arbitrators to treat similar cases in a similar fashion and to support

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[147] See Gabrielle Kaufmann-Kohler, "Le contrat et son droit devant l'arbitre international" in François Bellanger *et al*, eds, *Le contrat et son droit devant l'arbitre international: Proceedings of the Le contrat dans tous ses états : publication de la Société genevoise de droit et de législation à l'occasion du 125e anniversaire de la Semaine Judiciaire,* Berne, 2004 Staempfli; Schultz, "Secondary Rules" *Supra* note 143 at 66.

[148] For more information see Gabrielle Kaufmann-Kohler, "Arbitral Precedent: Dream, Necessity or Excuse? The 2006 Freshfields Lecture" (2007) 23:3 Arb Int'l 357. ["Arbitral Precedent"]

their reasoning by referring to other arbitral decisions. As Schultz puts it: "…prior cases have come within the purview of the regimes' secondary rules of recognition and have become sources of law, regardless of the fact that no formal legal rule compels arbitrators to do so, regardless of the fact that these precedents are not precedents, legally speaking."[149]

The question is whether or not the development of secondary rules among arbitrators as a community of transnational adjudicators has altered international commercial arbitration as an autonomous legal system.

As I briefly discussed above, according to Hart's theory of law, primary rules alone cannot constitute a legal system. The rules of behavior, therefore, need secondary rules in order to constitute a system. A primary rule "is a rule referring to behaviour, understanding by that only factual acts, that is, acts that do not create legal effects"; on the other hand, a secondary rule "may be defined as a rule referring to other rules, including in this the legal act by which the first rule may have been created."[150]

According to Hart's theory, a society may survive under the governance of only primary rules; however, it will show defects in many aspects, including uncertainty in the determination of rules, being static in adapting to the new circumstances, and ineffectiveness in imposing rules on its subjects.[151] Hart prescribes three mechanisms through which a normative order could form a perfectly functional legal system. The rule of recognition is proposed to recognize

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[149] Schultz, "Secondary Rules" *Supra* note 143 at 68.

[150] Van De Kerchove & Ost, *supra* note 15 at 17.

[151] Hart, *supra* note 110 at 88-91; Van De Kerchove & Ost, *supra* note 15 at 18.

the rules that belong to the system, and the rule of change is introduced to turn the static primary rules into dynamic ones in order to replace old rules by new ones. Finally, a legal system requires rules of decision, which enable the legal system to assess whether a rule is broken; and if it is, an appropriate sanction will be imposed on the subjects.[152]

Using Hart's theory, critics argue that international commercial arbitration has several defects in both primary and secondary rules; therefore, it does not deserve to be considered an autonomous legal system. They basically claim that the arbitral legal system has developed only secondary rules of recognition regarding procedural rules and lacks primary rules governing the substance of arbitral cases. Therefore, to rule on a case, the arbitrators have to borrow applicable laws from other systems. The other criticism is related to the rules of decision. It is said that arbitration does not have a mechanism of its own to enforce an award. Thus, arbitration has to depend on national legal systems to recognize and enforce an award.

One can respond to the criticisms about substantive law in many ways. First, many secondary rules of recognition directly affect the rules of conduct governing merits and awards. For instance, by considering the transnational nature of arbitration, interpretation methods can generate primary rules in regard to the substantive rules specific to arbitration. In addition, some scholars have introduced the *lex mercatoria* as substantive law for purposes of arbitration. However, the existence of the *lex mercatoria* is denied by some scholars, while

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[152] Hart, at 88-91; Van De Krechove & Ost, *Supra* note 15 at 18.

others express doubt to credibility of the *lex mercatoria* as law due to its lack of certainty, predictability, and effectiveness considered as essential characteristics of a law. Given that the *lex mercatoria* is a controversial and important topic for the development of the arbitral legal system, it is discussed separately in more detail in the next part. Finally, one may also argue that it is a positive aspect of arbitration that it gives parties the freedom to decide on substantive rules and permits arbitrators to determine substantive rules by a comparative, pluralistic, and trans-systemic method in order to determine the most appropriate law applicable to the merit.

The New Lex Mercatoria

It has been felt necessary to develop a transnational substantive law for the resolution of transnational disputes. There are two major reasons. First, national substantive laws are insufficient and incapable of solving modern and complicated international commercial disputes. This is because their aim is either to govern domestic commercial relationships or to protect the relevant nationals' rights in international transactions. Secondly, the complexity of application of the rules of conflict of laws generates many difficulties for arbitral tribunals to determine an applicable law.[153] Because of the uncertainty and unpredictability of national laws and the conflict of laws doctrines, the international arbitration community has tended to utilize comparative law, trade usages, and customs as

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[153] Klaus Berger, *The creeping codification of the lex mercatoria* (The Hague: Kluwer Law International, 1999) at 2.

well as the practices of international commerce and trade—the so-called *lex mercatoria*—as a substantive law in order to create a suitable substantive legal order to govern international disputes. William Park has explained the legitimate objectives of an a-national legal order to rule on arbitral cases; he explains that: "The proponents of lex mercatoria certainly have important and legitimate objectives: to discern rules for international commerce that conform to parties' expectations, and to avoid the trap created when the otherwise applicable national law appears uncertain, peculiar, dramatically amended since the date of the contract, or otherwise unpredictable and unjust in its application to foreigners."[154]

The definition and nature of the *lex mercatoria* are controversial. On the one hand, its existence has been questioned and described as a policy that is fabricated to guarantee international corporations' interests. On the other hand, it is argued that systematic use of the *lex mercatoria* by arbitral tribunals has transformed its nature and turned it from a "soft law" into an institutionalized legal order.[155] Notwithstanding the attacks on the *lex mercatoria* or philosophical differences about it, in practice, the *lex mercatoria* appears to have filled the legal vacuum in international commercial arbitration. It provides the international arbitration community with a set of general principles, rules, and standards to govern merits in arbitral cases. Arbitrators have used it as substantive law, for interpretation purposes, and for adjustment of national laws in accordance with

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[154] Park, *supra* note 37 at 529.

[155] Ralf Michaels, "The True Lex Mercatoria: Law Beyond the State" (2007) 14:2 lnd J Global Legal Stud 447 at 448.

the international nature of arbitration.[156]

The sources of the *lex mercatoria*, in the broad sense, are various and include international trade usages, general principles of law, standard form contracts, general conditions and terms, and codes of conduct. We should differentiate between old and new notions of the *lex mercatoria*. The old *lex mercatoria* comprises the trade customs developed among merchants from ancient times until the present day. However, the new *lex mercatoria* is the creation of international legal practitioners to cope with problems that domestic law may generate in international commercial dispute-resolution processes. Probably, this is why it is difficult to come up with a comprehensive definition, for the entity has been defined in various forms and conceptualized in different ways.

However, the *Lex Mercatoria* has some definite characteristics that most of the commentators agree on. First, it is a-national because it is "a law which has arisen spontaneously and developed on the edge of national legislations"; secondly, it is transnational because "it is a law common to commerce all over the world."[157]

Despite agreement on its characteristics, the new *lex mercatoria* has been conceptualized in different ways, three of which seem important.

The first approach conceptualizes the *lex mercatoria* as a set of rules, so-

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[156] Ibid.

[157] Jean Francois Poudret & Sébastian Basson, *Comparative Law of International Arbitration* (London: Sweet & Maxwell, 2007) at 596, para. 592.

called "Rules of Law" without considering it a transnational legal system.[158] The second approach conceptualizes the *lex mercatoria* as a "method of decision making". The focus of this approach is on the source of the *lex mercatoria* as opposed to its content as a list of legal principles. According to this approach, arbitrators derive the substantive solution of a legal dispute from a "comparative law analysis."[159] This, in turn, provides more flexibility to chose a widely accepted and more appropriate rule among the relevant legal systems. Schultz uses a phrase that describes very well this approach: "it is conceived of as a normative process towards the selection of norms."[160] Accordingly, the source of binding force of the *lex mercatoria* is not derived from a national legal system; but rather, "the rules of the lex merctoria have a normative value which is independent of any national legal system."[161] In other words, the *lex mercatoria* is an independent normative order by which arbitrators determine—on a case-by-case basis and according to party autonomy—which norms are in conformity with the system and appropriate for application.

The third approach considers the *lex mercatoria* as an independent legal system. According to this notion, the *lex mercatoria* has created it own constitutionalization outside the state and has become a transnational legal system. Regarding the source of the judicial mater of the *lex mercatoria*, there are

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[158] Schultz, "Lex Mercatoria" *Supra* note 72 at 678, para. 671; see Simon Roberts, "After Government? On Representing Law Without the State" (2005) 68:1 The modern law review 1.

[159]Gaillard, "Transnational Law" *sura* note 11 at 62.

[160] Schultz, "Lex Mercatoria" *Supra* note 72 at 673.

[161] Michael Mustill, "The New Lex Mercatoria: The First Twenty-five Years"(1988) 4:2 Arb lnt'l 86 at 110.

different theoretical approaches. From the natural law perspective, the *lex mercatoria* is a set of inherently legitimate and morally valuable rules. According to Carbonneau, "this body of law consists of three sets of rules: universally acknowledged, natural-law-type principles, national legal principles which mirror the pragmatic ethic of the community of international merchants."[162] From the positivist perspective, as Gaillard describes it, the *lex mercatoria* has been recognized as an appropriate legal order by some states to be applied by arbitrators, for instance by French, Swiss, and Dutch arbitration law. Therefore, states' recognition of the *lex mercatoria* has been considered grounds for legitimization of the applicability of the *lex mercatoria*.[163] Gaillard adds that the *lex mercatoria* has four crucial characteristics of any valid legal system. Those characteristics are "completeness", which means that the system is capable of providing answers to any legal issue; "structured," which indicates that "A legal system is an organized set of rules, with various levels of generality and close ties between rules belonging to those levels"; "ability to evolve," which refers to its ability to assess the "outcome of any diverging views that may arise"; and "predictability," which means that all of these charcteristics can be found in the *lex mercatoria*.[164] Schultz has analyzed the positivist approach to the new *lex mercatoria* using Hart's "secondary rules of recognition theory."[165]

Accordingly, a norm, in order to be considered legal, has to be "re-

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[162] Carbonneau, *supra* note 98 at 16.

[163] Gaillard, "Transnational Law" *supra* note 11 at 65.

[164] Ibid.

[165] Schultz, "Lex Mercatoria" *Supra* note 72 at 685; Hart, *supra* note 110 at 113.

institutionalized" or recognized by a legal system. This idea differs from the previous positivist approach in certain ways. First, recognition of a norm by other legal systems cannot be a legitimate ground in favor of the legal status of a set of norms. In other words, a state's confirmation cannot grant the character of law to a norm in another legal system. Schultz argues that any given legal system is inherently incapable either to recognize or to disqualify other legal system.[166] Therefore, the recognition of the *lex mercatoria* as a legal system by some national legal systems cannot validate the *lex mercatoria*'s legal character. Consequently, a set of rules, in order to be considered law, has to belong to a legal system of its own and must be acknowledged by the officials of that legal system.

Despite the theoretical and doctrinal complexity involved, I would like to emphasize two important points. The first point is that regardless of what theorists or scholars say about the legality of the *lex meratoria* based on the traditional legal concepts, the *lex mercatoria* has been used by and is accessible for parties and practitioners. In addition, there is an increasing trend among various practitioners to develop a neutral and transnational *lex mercatoria* to govern international transactions in specific industries. For instance, Berger reports that "the development of a '*lex petrolia*' for the international oil-industry, a '*lex numerica*' or '*lex informatica*' for international data interchange, or '*lex constructionis*' for the international construction industry, which reveals that the transnationalization of commercial law has already transcended the traditional

[166] Schultz, "Lex Mercatoria" *Supra* note 72 at 687.

boundaries of general contract law."[167] The *lex mercatoria* has found its way to arbitral awards. For instance, the sole arbitrator in ICC Award No. 8385 (paragraph 1066) states: "the application of international principles offers many advantages. They are applied neutrally and independently from particular national law. They take into account the needs of international relationships and permit a fruitful exchange between the systems when excessively related to conceptual distinctions and for who seeks a just and practical solution for the case in hand. Therefore, this is an ideal opportunity for applying what is increasingly called lex mercatoria."[168] Therefore, in my view, the focus should not be on the theoretical analysis of the *lex mercatoria*; instead, one should consider the practical importance and market needs that recognize the *lex mercatoria* as a set of reliable and neutral rules that can be used as a basis to settle international disputes.

(b) Legality and Justice: "Procedural justice" and the Fullerian "inner morality of law"

Legality and justice are two very closely related concepts. It is true to say that the ultimate goal of a legal system is to establish justice. A legal system should be analyzed as to whether or not it has the minimum qualities to meet its

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[167] Berger, *supra* note 153 at 230.

[168] U.S. company v. Belgian company, (1995), 124 JDI 1061 ICC Award No. [Translated by author] Original text: "L'application de principes internationaux offre beaucoup d'avantages. Ils s'appliquent uniformément et sont indépendants des particularités de chaque droit national. Ils prennent en compte les besoins des relations internationales et permettent un échange fructueux entre les systèmes parfois exagérément liés à des distinctions conceptuelles et ceux qui cherchent une solution juste et pragmatique de cas particuliers. C'est donc une opportunité idéale pour appliquer ce qui est de plus en plus nommé lex mercatoria."Online: <http://www.trans-lex.org/208385.>

objective. Therefore, it is crucial to determine an appropriate concept of justice that will eventually help us to assess the validity of a legal system.

It is a common expression among practitioners that realization of justice in a society relies on the equal application of the law without any discrimination. In other words, it is a simplistic notion of justice that conceptualizes justice as conformity with the law.[169]

The main question is how the practical notion of justice can be used to assess the legality of the arbitral normative regime. Thomas Schultz believes that the only relevant notion of justice for a lawyer is compliance with the law. He states:

> The understanding of justice in the sense of conformity to law (*Gerechtigkeit als Rechtsmässigkeit*) may be the dominant mode among lawyers in dealing with questions of justice. This approach is based on the tenet that justice (*Gerechtigkeit*) can only be found in conformity to law (*Rechtsmässigkeit*); it conceives of justice qua justice according to law, where law stands for the utterances of the sovereign—the law of the state.[170]

He continues by saying that the general trend among lawyers is that law is

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[169] At first glance, such a concept seems a fallacy in conceptualizing law because the premise (law) is used to prove the conclusion (justice) and the conclusion (justice) is used to prove the premise (law). One may find a logical flaw in the legality and justice theory. In the theory, legality is seen as an attribution of a normative order that is just, and justice has is conceived as conformity to law. According to the theory, the suggested definition of law seems to be a vicious circle. But, by further considerations, the logical flaw can be resolved.

[170] Thomas Schultz, "The Concept of Law in Transnational Arbitral Legal Orders and some of its Consequences" (2011) 2:1 Journal of International Dispute Settlement 59 at 66. ["Concept of Law"]

subject to sovereignty, i.e. a state; and therefore, lawyers depend on sense of practical justice, which is relying on legislation rather than on the deep meaning of law.

According to this approach to justice, there remain two choices for assessing the legality of the arbitral regime: either to take justice as focusing on national laws and international conventions or to adopt an understanding of justice built on the foundation of national courts' decisions. Both approaches seem inappropriate for legitimization of the arbitral legal system. The former supports the idea that national laws and international conventions have approved a greater autonomy to be given to international arbitration by states. This notion of legality is not acceptable because it would appear that autonomy is not something that states can give to the arbitral legal system; in contrast, autonomy is a qualification that a legal system should have. The legality of law in the latter choice is considered "relative legality" because some national courts may recognize a non-state normative rule as law and others may not.[171]

Substantive justice is the other approach to assess the legality of arbitral system. Although it has some advantages over practical justice, it still has some problems. Given the heteroarchical nature and lack of higher standards in anational rules, substantive justice gives a flexible and analytical framework to assess the credibility of the arbitral legal system. However, due to the existence of diverse legal traditions in the transnational rules, the substantive approach will fail. Moral principles of legal pluralism, such as being unbiased and neutral, do

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[171] Ibid at 67-68.

not allow us to assess the credibility of the arbitral legal system as a just regime based on a particular type of substantive justice.[172]

The theoretical flaws and practical shortcomings of substantive justice have induced some scholars to adopt procedural justice was a way to assess the arbitral legal regime. As Schultz states:

> The inherent variegatedness of conceptions of substantive justice requires that we dispense with arguments relating to the regulative quality of an arbitral regime on the basis of the contents of its rules or the way in which it redistributes resources and limit ourselves to procedural aspects of such a rules system. The question then simply is whether such a regime truly allows to "predict and plan."[173]

He then concludes that formal justice is an appropriate criterion to assess the legality of the arbitral legal system. According to formal justice, the arbitral normative system does not deserve to be considered as law and a legitimate autonomous legal system unless it is based on the procedural justice theory; its proceedings operate in a just manner. Now the question is: what makes a procedure of a legal system just? Or what are the crucial procedural characteristics of a normative system for it to be considered law? Or again, what are the formal qualifications for such a legal system to be realized as an autonomous legal system?

As I mentioned in the previous part, Professor Fuller has introduced "procedural natural law" methods to assess the legality and credibility of any

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[172] Ibid at 68-69.

[173] Ibid at 70.

normative order. He has named it the "internal morality of law," which basically means that the main objective of a legal system is to conform to standard procedural principles, regardless of their substance. He lists eight failures that prevent one from making laws. Then he concludes that in order to establish a legal system, one has to overcome those failures, and to do so he comes up with eight solutions.[174]

The eight solutions are the basic procedural principles necessary for a normative system to be considered law. Arbitrators and scholars have exploited the Fullerian procedural qualities of a regulatory system to analyze the legality of the arbitral legal system.

On the basis of the "inner morality of law," the legality of such a normative system has been refuted. Generally, it is said that the arbitral legal system as an "outcome-centred mode of regulation" suffers from procedural deficiencies such as "generality," "steadiness," and "public ascertainability" that prevent it from evolving into an independent legal system. The critics epitomize Fullerian theory as lacking three important systemization attributes of international arbitration: namely, precedent, publication of international commercial arbitral awards, and a mechanism to unify arbitral awards.

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[174] The eight solutions for legality of a normative order: "P1: governance by general norms, that is the generality of expression and application of the rules that are part of the system; P2: public ascertainability, or the public promulgation of the rules of the system; P3: prospectivity, meaning the non-retroactivity of the rules of the system; P4: perspicuity, that is the formulation of the mandates provided by the legal system in lucid language; P5: non-contradictoriness and non-conflictingness, in other words the normative coherence of the legal system; P6: compliability, that is the near absence of unsatisfiable behests; P7: steadiness over time, which calls for 'limits in the pace and scale of the transformations of the sundry norms in a legal system; P8: congruence between formulation and implementation, in other words that the publicly promulgated rules are actually applied and are applied impartially." Ibid at 72; Fuller, *supra* note 121 at 33-41.

Gaillard, Fouchard, and Goldman also conclude, in a relatively similar way, that:

> Three conditions must be satisfied or, rather, three obstacles surmounted, for arbitral awards to have the same sort of influence as court decisions. First, courts must not have reviewed the substance of the decisions reached in the awards, as that would cause them to be dependent on national legal systems. Second, the various decisions reached on a particular issue should display some degree of homogeneity. Third, the decisions should be accessible to the public.[175]

I set aside the first condition because the subject is discussed in the first part of the thesis. The second and third conditions raise the problem of transparency in international commercial arbitration. Transparency in international arbitration gives rise to two important topics: namely, precedent and publication of awards.

Before arguing for the transparency of arbitration as an essential condition for its systematicity, it is necessary to discuss the justifiability of the Fullerian black-and-white approach to the concept of law. Basically, listing certain characteristics to assess legality of a normative system underplays the fact that the transformation and development of a normative system to a legal system occurs gradually. According to Schultz, "The evolution from a social normative to a legal system takes place progressively; there are many intermediate stages between a typical social ordering and a full-blown legal system."[176] He also concludes that

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[175] Fouchard *et al*, *supra* note 72 at 183.

[176] Thomas Schultz, "Private legal systems: what cyberspace might teach legal theorists" (2007) 10 Yale JL&T 151 at 168. ["Private Systems"]

not only are normative rules transformed into a legal system gradually over time, but also a relatively simple legal system constantly develops into a more sophisticated one. It is worth mentioning here Van de Kerchove and Ost's conclusion about legal systems in their famous book *The Legal System between Order and Disorder*. They conclude that adopting two extreme concepts of a legal system, namely a system that is "lacking any principle of cohesion" and a system that is "perfectly systematized," "can only be an obstacle to a satisfactory knowledge of law."[177] They also suggest a modest critical concept of law, that is, the "plural and relativistic conception of systematicity in law, situating it resolutely between order and disorder."[178] According to this view, a dogmatic theory of law does not fit international arbitration because the arbitral legal system as a relatively newly-emerged legal system has to go through a number of stages in order to become a perfectly transparent, consistent, and predictable legal system. In addition to that, Fuller's eight criteria apply to the classical methods of making law, such as legislation. They are not meant to be applied to a case law system or in a legal system in which precedents are the main source of law. The results obtained in case law are different from those in the legislative process. As Professor Gélinas believes, the age of communication, information and globalization has changed the classic legislative methods and the assessment of the rule of law. The old kind of legislative method has lost its centrality; instead,

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[177] Van De Krechove & Ost, *Supra* note 15 at 170-171.

[178] Ibid at 171.

more credence is now being given to the rationality of case law.[179] Therefore, regarding the nature of the arbitral legal system, which is case-law based, the application of Fuller's criteria to the assessment of the credibility of rules of law does not seem justifiable.

(i) Precedent in International Commercial Arbitration

The arbitral legal system has been criticized for its lack of a legislative mechanism. It is argued that arbitral awards do not have precedential power as a replacement for a legislative mechanism. This would be the mechanism that could generate general rules from arbitral awards, the rules that are being followed by other tribunals at least for a certain period of time. There are different approaches to criticizing international commercial arbitration for its lack of precedential power.

It has been claimed that international arbitration operates on an ad hoc basis and is designed simply to resolve disputes; therefore, arbitral awards are not meant to constitute the jurisprudence that would be followed by other kinds of arbitral tribunals.[180] It is also argued that normative order in an outcome-centered legal system, like the arbitral legal system, are "situation-specific directives" that cannot be generalized to other cases or generate generating general guidelines.[181] Moreover, they are retroactive norms that are undetermined until the final award

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[179] Fabien Gélinas, "Virtual Justice and the Rule of Law"in Karim Benyekhlef & Pierre Trudel, eds, *État de droit et virtualité*, (Montréal: Éditions, Thémis, 2009) 293-319 at 306-307.

[180] Schultz, "Concept of Law" *Supra* note 170 at 73-74.

[181] Ibid.

is rendered. Consequently, they are not capable of generating general norms or precedents. Schultz states:

> A normative regime based on arbitral awards requires certain mechanisms that ensure the possibility for the addressees to generalize the normative bearings of an award, effectively grasping norms that transcend each individual case, so that they can apprise themselves of the rules under which the consequences of their present and future actions will be assessed. Cognate situations must be made normatively relatable to one another, across cases and over time.[182]

He believes that international commercial arbitration does not have such mechanism to create precedents.

In some kinds of arbitration, such as investment, sports, and domain-name arbitration, it is claimed that in order to bring about more consistency and predictability, it is crucial to rely on previously decided cases. Statistics have also proved the role of precedent in these types of international arbitrations.[183] Contrary to that situation, however, it has been argued that international commercial arbitration does not need precedents because arbitrators in commercial arbitration resolve cases based on facts that are related exclusively to the case in hand. In addition, there is an expectation that they will take into account the parties' autonomy and their needs regarding how to resolve the disputes. Kaufmann-Kohler says:

> In commercial arbitration, there is no need for developing consistent rules

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[182] Ibid at 76, para 74.

[183] See Kaufmann-Kohler, "Arbitral Precedent" *supra* note 148.

> through arbitral awards because the disputes are most often fact- and contract-driven. The outcome revolves around a unique set of facts and upon the interpretation of a unique contract that was negotiated between private actors to fit their specific needs.[184]

It would seem that the idea of the existence of the arbitral legal system is in absolute contrast to these arguments, for such an individualized and isolated normative order does not deserve to be called legal system. It is fair to say that a legal system without a mechanism to generate general binding rules could not be efficient. "Precedential force" of arbitration awards is introduced as a crucial requirement for satisfying the legality of the system. As Schultz specifies, "precedent" satisfies four of the Fullerian principles of legality: namely, "governance by general norms," "public ascertainability," "prospectivity," and "steadiness through time."[185]

In order to be able to reach a conclusion about the existence of precedent in international commercial arbitration and the precedential power of arbitral awards, we need first to define "precedent" according to the nature of a transnational legal system and secondly to apply the definition to actual practices.

The term "precedent" as used here originates in national legal systems, particularly in the common law system. Due to the differences between the national and transnational legal systems, it seems that traditional definitions and conditions of precedent are not compatible with international arbitration. The

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[184] Ibid at 375-376.

[185] Schultz, "Concept of Law " *Supra* note 170 at 72.

hierarchical structure of courts helps to create binding rules by higher courts that lower courts are obliged to follow. In addition, national legal systems usually have a mechanism to officially unify, codify, and classify their leading decisions. International commercial arbitration as a heteroarchical legal system does not have the traditional mechanism to unify and classify arbitral awards. Therefore, the differences between the systems require a conceptualization of precedent according to the nature of international arbitration and how it works in actual practice.

Using empirical support, Barton Legum has defined a precedent in international arbitration "as any decisional authority that may reasonably serve to justify the arbitrators' decision to the principal audience (i.e. the public) to that decision."[186] He continues, precedent in international arbitration is relative. Legal practitioners, academics, and arbitrators look at precedent in different ways. A legal counsel is looking for any arbitral award to support his or her claims, while arbitrators seek any award to justify their decisions. Given the diversity of the international arbitration community from different jurisdictional backgrounds, the value of precedent becomes relative.[187]

In addition, it seems that the existence of precedent is not the main concern, because practices support the importance of the role arbitral awards play. The main question is how precedents are created and how other tribunals in international arbitration follow them. Alexis Mourre states:

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[186] Barton Legum, "The Definition of "Precedent" in International Arbitration", in Emmanuel Gaillard & Yas Banifatemi, eds, *Precedent in international arbitration* (Huntington, N.Y. : Juris Pub., 2008) at 14. [*Precedent*]

[187] Ibid at 10.

> These decisions are referred to by other arbitrators, and they may in certain cases persuade future tribunals to adhere to previous solutions. Arbitral precedent is no more and no less than this capacity of past arbitration awards to convince future tribunals to adhere to the solution they embody. The proper question should therefore not be whether arbitral precedent exists, but how and when it does operate.[188]

The precedential force of arbitral awards is the result of communication among the international arbitration community. The awards that get published are closely watched by the international arbitral society. Arbitrators, lawyers, and scholars analyze their reasoning and interpretations. The exchange of ideas against and in favor of an award eventually generates a balanced outcome and relative consensus among the members of society, which in turn could persuade parties and arbitrators to be inspired by such awards in future cases. In practice, arbitral tribunals are usually faithful to the reasoning and interpretation of the previously published arbitral awards. Lawyers and arbitrators support their claims and decisions by referring to previously resolved arbitration cases.[189] Even if arbitrators do not cite other arbitral cases in their awards, this does not mean that other arbitral awards do not inspire their decisions. In most cases, arbitrators share

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[188] Alexis Mourre, "Arbitral Jurisprudence in International Commercial Arbitration: The Case For a Systematic Publication of Arbitral Awards In 10 Questions…"(28 May 2009) Kluwer Arbitration Blog, online: <http://kluwerarbitrationblog.com/blog/2009/05/28/arbitral-jurisprudence-in-international-commercial-arbitration-the-case-for-a-systematic-publication-of-arbitral-awards-in-10-questions%E2%80%A6/ >

[189] It has also been an object of criticism that statistics do not show a significant number of cases that refer to other arbitral cases. For instance, a study of 190 arbitral awards showed that only 15 percent of them cited other arbitral cases. Kaufmann-Kohler, "Arbitral Precedent" *supra* note 148 at 363.

a common logic and ground to rule on the case because they are part of a large community that shares knowledge and information within itself. François Perret confirms this approach by saying that:

> [F]or the purpose of deciding on international commercial disputes, particularly on contractual disputes, arbitrators are not a *terra incognita* but in a legal environment which, because it is familiar to them, may constitute a common ground for their decision. It is therefore not surprising at all to note the homogeneous character of arbitral awards deciding on the same point of law, and that is, in my opinion, sufficient to admit the existence of arbitral case law.[190]

As Professor Gélinas suggests, reasoning is the "persuasive authority" and the source of the power of precedent in arbitration, whereas in national legal systems the hierarchy of the tribunals confers formal authority on the courts' decisions. He states: "The lack of a hierarchy of tribunals creates a situation in which a decision becomes a leading case not because of some power formally granted to the arbitrators or status conferred on their awards, but by virtue of the authority, now laid bare, wielded by their reasoning."[191]

Christopher R. Seppala, in analyzing several arbitral cases, demonstrated that FIDIC (International Federation of Consulting Engineers) arbitration provides

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[190] Gaillard & Banifatemi, eds, *Precedent sura* note 186 at 34; Christopher Seppala, "The Development of a Case Law in Construction Disputes Relating to FIDIC Contracts"in Emmanuel Gaillard & Yas Banifatemi, eds, *The International Construction Law Review* (Huntington, N.Y. : Juris Pub., 2008) at 67.

[191] Fabien Gélinas, "Investment Tribunals and the Commercial Arbitration Model: Mixed Procedures and Creeping Institutionalization" in Mark Gehring, Cordonier Segger & Marie-Claire, eds, SUSTAINABLE DEVELOPMENT IN WORLD TRADE LAW (The Hague: Kluwer Law International, 2005) 577 at 583.

a good example of the application of arbitral precedents. FIDIC contracts have emerged from business practices, and the disputes arising from them are resolved mostly through arbitration. Seppala, through his analysis of some arbitral awards, points out that they are inspired by similar and previously resolved cases in the domestic courts of a country that has a close relationship with the country whose legal system is being chosen for the applicable law.[192] Therefore, an arbitral award is the result of a comparative analysis of legal solutions of several national and transnational legal systems that have dealt with relatively similar cases.

In addition, a comprehensive statistical and empirical study of 207 investment arbitration cases showed that most arbitral tribunals tend to cite other cases.[193] The study created a "searchable precedent matrix" including ICSID (International Centre for Settlement of Investment Disputes) and non-ICSID arbitral cases. By examining the results, one finds that in the majority of cases, the reference was made to more than one arbitral award.[194]

As a final remark, one should also bear in mind that arbitration is contractual in nature; therefore, arbitrators have to achieve a balance between consistency and predictability, which demands following previously decided cases, and flexibility, which demands responding to the specific needs of particular parties or the requirements of the business market. It is the parties' expectation that their case will be resolved on the basis of internationally

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[192] Seppala, *supra* note 190 at 74.

[193] JP Commission, (2007) Precedent in Investment Treaty Arbitration: The Empirical Backing TDM 5, online: < www.transnational-dispute-management.com>.

[194] See, e.g. JP Commission; "Table A: Precedent in ICSID Arbitration 1972 - 2006" TDM 5 (2007), online: <www.transnational-dispute-management.com>.

recognizable rules and principles that have been confirmed by other tribunals. Alexis Mourre has described this very well: "The driving force of arbitral precedent is rather the arbitrators' desire to meet the parties' legitimate expectation that their dispute will be resolved by international adjudicators according to internationally accepted procedures and from an international perspective."[195] Conversely, arbitrators should be flexible in ruling on a case in accordance with what parties may agree during the arbitration process and what they believe is the best solution regarding the case's circumstances and the parties' demands. Therefore, arbitrators should have a certain amount of discretion as to when and how apply precedents in the case at hand to balance consistency and flexibility.

(ii) Transparency vs. confidentiality

Studying different approaches to theorizing the arbitral legal system reveals that the systematization and systematicity of international commercial arbitration depend on the transparency of the arbitration process. Public accessibility to arbitral awards is a fundamental prerequisite to the creation of arbitral precedents and for the evolution of international arbitration as a legal system. Alexis Mourre believes that the reason why arbitrators do not refer to arbitral precedents should be sought in the question of the transparency of

[195] Alexis Mourre, "Arbitral Jurisprudence" *supra* note188.

international commercial arbitration.[196]

Publication of awards in international commercial arbitration has faced two main problems. First, it is argued that they are not published systematically and sufficiently. Secondly, it has also been stressed that confidentiality in commercial arbitration is the main obstacle to making the awards accessible to the public. I am going to discuss these two issues below.

Traditionally, arbitral awards in ad hoc commercial arbitration are not published. Given that there is no data about the number of ad hoc arbitral cases, it is impossible to conduct a statistical analysis to find out what percentage of non-institutional awards has been published. However, it is apparent that the portion of published ad hoc awards is too small to be considered representative of the arbitral decisions.

A survey about published awards in a certain area indicated the probability that the majority of the arbitral awards are hidden. This survey of the awards relating to the CISG (Convention on the International Sale of Goods) revealed that only 20 percent of these awards were published.[197] Another study, conducted by Christopher R. Seppala, showed that only 40 awards related to FIDIC have been published. Given the huge number of construction arbitration cases under FIDIC, 40 is not a significant number. [198] The study of institutional arbitration produces the same result. Arbitral institutions publish less than 20 percent of the

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[196] Alexis Mourre, "Precedent and Confidentiality in International Commercial Arbitration: the Case for the publication of Arbitral Awards" in Gaillard & Banifatemi, *Precedent supra* note186 at 53.

[197] Kaufmann-Kohler, "Arbitral Precedent" *supra* note 148 at 362.

[198] Seppala, *supra* note 190 at 34.

awards. The ICC as a leading institution has a clear policy on publication of awards and publishes its awards regularly in a number of languages several times a year. Statistics show that between 1974 and 2007, the ICC published only 15 percent of its awards.[199]

While the criticisms have targeted the low rate of publication of arbitral awards, there are several arguments that should be taken into account. It should be borne in mind that the purpose of the publication of awards is to make valuable awards accessible to the public. A valuable award is the one potentially capable of generating a legal order, leading to a solution, and demonstrating justifiable reasoning that can be used in future cases. One may argue that the quantity of published awards is low because not all arbitral awards deserve to be published. Many arbitral cases are resolved according to parties' reconciliation or amiable composition. These kinds of awards are merely fact-based and relate exclusively to the case at hand, so they are inherently unable to create precedents.

What matters for reliable jurisprudence is quality not quantity. This leads to the next argument. What we know today as an arbitral legal system is the result of the small portion of the awards that have been publicized. The quantity and quality of the published awards in terms of reasoning, interpretation, and legal resolution are enough to generate general rules. However, given the important role of transparency in the systematization of international commercial arbitration, they are not sufficient. This is probably the reason why transparency in arbitration processes and publicizing arbitral awards is an increasing trend among the international arbitration community. The number of collected books and online

[199] Kaufmann-Kohler, "Arbitral Precedent" *sura* note 148 at 362.

databases is constantly increasing. Some people have suggested creating and developing international databases similar to CLOUT (Case Law on UNCITRAL Texts)[200] to promote awareness and to provide the international arbitration community with access to centralized databases.[201] The privacy and confidentiality of commercial arbitration are, however, conceived as serious obstacles to transparency in publicizing arbitral awards. It is argued that given the confidentiality of arbitral awards, many of them never get published; and thus, it is not possible for the international arbitration community to be aware of these awards. This is a critical concern, which affects the practicability of a system of precedent in arbitration. Confidentiality also makes arbitration attractive for the arbitration users, where business information remains private. In contrast to what has been argued, it seems that confidentiality is neither inherent in the nature of international commercial arbitration nor against parties' privacy.

The privacy of arbitral hearings and the confidentiality of the information relating to proceedings, evidence, documents, and parties' identities are meant to protect commercially sensitive information from access by third parties. The sources of arbitrators' and parties' obligations (or rights) to keep information under cover vary. Parties may agree on confidentiality explicitly or by referring to national or transnational arbitration rules that prevent disclosure of information.[202] The main question is whether an overriding general rule exists to

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[200] Case Law on UNCITRAL Texts, online: <http://www.uncitral.org/uncitral/en/case_law.html>.

[201] Mourre, "Arbitral Jurisprudence", supra note 188.

[202] Ileana M Smeureanu, *Confidentiality in International Commercial Arbitration* (Alphen aan den Rijn: Kluwer Law International, 2011) at 8-25.

support confidentiality even if there is no implied or expressed consent of parties. In other words, is confidentiality an essential characteristic of international arbitration? Neither a reasonable theoretical foundation nor any national and transnational statutory ground can be found to prove that confidentiality is an essential characteristic of arbitration. Therefore, the answer seems to be negative. The main function of confidentiality is to protect business information when it is considered necessary to do so by the parties. It is very hard to claim that arbitrators and parties have an obligation of confidentiality if there is no expressed consent. This notion is reflected in transactional arbitration rules. The new version of the 2012 ICC rules does not mention the duty of confidentiality on the part of parties or arbitrators. Therefore, it puts the responsibility on the tribunal to decide about the confidentiality of a proceeding. While the ICC has a policy to publish its awards, the institution does consider the parties' concerns about confidential information and documents.[203] UNCITRAL Arbitration Rules also do not mention confidentiality in arbitration, and Article 34(5) of the UNCITRAL Arbitration Rules emphasizes only the parties' consent: "An award may be made public with the consent of all parties.…"Some national arbitration rules also mention business sensitivity as the main concern and indicate that there is no jurisdiction that considers confidentiality as belonging to the nature of international commercial arbitration.[204] For exmaple, Section 5 of Norway's Arbitration Act states: "Unless the parties have agreed otherwise, the arbitration proceedings and the decisions

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[203] Mourre, "Arbitral Jurisprudence", supra note 188.

[204] Smeureanu, *supra* note 202 at 20.

reached by the arbitration tribunal are not subject to a duty of confidentiality."[205]

One thing needs to be added to the above discussion: in order to protect sensitive information, arbitral awards can be redacted and published after elimination of the sensitive information and after a reasonable period of time.

To conclude, I think that confidentiality should not be considered a serious obstacle to publicizing awards. The quality of the small portion of published awards can be considered representative of the arbitral desicions.

C. The Social Scientific Concept of Law

From studying the traditional and modern concepts of law, it seems that debates on the concept of law from the philosophical and jurisprudential points of view never end. The reason for this kind of ongoing and endless debate may be sought in the approaches that are taken by theorists. Legal theories are not able to predict social, economic, and technological upheavals. They are not capable of imagining how the power structure will take shape when new factors come into existence. It is beyond imagination's capacity to figure out how unpredictable factors will affect the concept of law in order to conceptualize an inclusive notion of law. Therefore, considering the evolving nature of law as a social phenomenon, in my view, assessment of the legitimacy of a new legal phenomenon by means of old legal theories will result in uncertainty. In addition, it seems irrational to

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[205] *The Arbitration Act of 14 May 2004* (2004) [ARCHIVED] in Jan Paulsson (ed.), *International Handbook on Commercial Arbitration*, Kluwer Law International 1984 (Last updated: June 2008, Supplement No. 52) pp. 1-16; online: <http://www.kluwerarbitration.com/document.aspx?id=ipn30336>.

assess the legality of social norms in a society by criteria that are tailored for other societies' norms. The issue is even more problematic when the formal structures of the societies are different. For instance, positivists' theories have been established to theorize a state-based and hierarchical legal system. Therefore, applying such theories of other societies that do not have the same characteristics does not yield justifiable criteria. Thus, Tamanaha observes: "Application of the state law model would result in the conclusion that many societies (historically speaking) did not have law."[206] This conclusion would apply to the anational rules as well, given that the positivist approach would result in the refusal to acknowledge the existence of law beyond nation-states. Endless disagreements over the concept of law in both traditional and modern theories and the shortcomings of theories of law have led to the emergence of a new approach to theorizing law, namely, the social scientific concept of law.

Unlike the traditional and modern concepts, the postmodern concept of law has shifted its focus to scientific experiments and empirical analysis of law as a social phenomenon. According to the scientific approach, all collective societies have law. As an anthropologist concludes, "no society is without law."[207] Luhman states:

> All collective human life is directly or indirectly shaped by law. Law is, like knowledge, an essential and all-pervasive fact of the social condition. No area of life—whether it is the family or the religious community,

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[206] Brian Z. Tamanaha, "An Analytical Map of Social Scientific Approaches to the Concept of Law" (1995) 15:4 Oxford J Legal Stud 501 at 501.

[207] Sally Falk Moore, *Law as process, an anthropological approach* (London: Routledge & Kegan Paul, 2000) at 215.

> scientific research or the internal networks of political parties—can find a lasting social order that is not based on law. Collective social life embodies normative rules that exclude other possibilities and lay claim to be binding with a degree of success.[208]

Human beings are social, and law is the result of human interactions in the society. It does not suffice to rely on human morality or on states' actions to understand the nature of law. In order to conceptualize law, one should scrutinize human interactions in a specific society.

The social scientific approaches give autonomy to the concepts of law and legal system; this autonomy negates the necessity of associating legality with states' sovereignty. This position has given theorists an opportunity to analyze the legality of the anational rules of the transnational communities.

Gunther Teubner as a legal scholar and sociologist is well known for his social theory of law. According to him, "law" is an "autopoietic system". In line with "autopoietic system" theory, law is not established by an external authority; it unfolds from the conventional nature of its own "positivity" or "self-reference." He also explains various ranges of self-reference: for example, "self-observation," "self-organization," "self-regulation," "self-production," "self-maintenance," and "autopoiesis" (self-creation), that are essential for a legal system to realize its systematicity and maintain its systematization.[209] Law, therefore, is an open and adaptive system, in the sense that it is affected, adjusted, and verified by its own

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[208] Niklas Luhmann & Martin Albrow, *A Sociological Theory of Law* (London: Routledge & Kegan Paul, 1985) at 1.

[209] Gunther Teubner & Zenon Bankowski, *Law as an Autopoietic System* (Oxford: Blackwell, 1993) at 19.

environment. One may argue that there is a paradox of circularity due to the self-referentiality of law, but the paradox exists even in a constitutional and hierarchical legal system, insofar as a state has to invent and legitimize itself. According to Teubner, circularity should not be seen as an intellectual flaw. In fact, moving in a circular directions is considered a creative and exploratory social phenomenon that reproduces ("hard operation") and observes ("soft operation") itself.[210]

Transformation and evolution of law in such a system is the result of mutual interaction, reciprocal pressure, and reconciliation of divergent ideas and expectancies within and among subsystems. Indeed, "law" strengthens its regulatory capability to the extent that it propels its normative orders and procedures towards "a theory of social autonomy and structural coupling."[211]

In the international context particularly, in the post-pluralism era,[212] it can be argued that anational rules are self-valued legal order. Multiple transnational sectors, for instance multinational enterprises and unions, as members of a global "civil society", have been generating a sort of transnational body of law, e.g. the *lex mercatoria*, labor law, human rights law, ecological law, and sports law, independently from states.

Furthermore, in the modern globalization process, law is a non-state and fragmented experience that is the result of functional "communicative networks" among the economy, culture, academia, and technology. For the purpose of

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[210] Ibid at 23.

[211] Ibid.

[212] Three eras of transnational law can be distinguished: namely, colonialism, pluralism, and globalism.

legitimacy and accountability, one should bear in mind that with the globalized legal order the focus has shifted from "structure to process, from norm to action, from unity to difference," and from function to the "binary code legal/illegal."[213]

The same approach has been taken by Ladeur in order to legitimize non-state transnational law as a rational and self-organized international project. In Ladeur's idea, postmodern global administrative law (emphasis on "law") is the result of a shift in the domestic legal system from legislating methods towards the market-based multi-layer normative orders to the point that the private sector has found more autonomy and independence than its creator. It is the same in public organizations, which have been characterized as "self-organization" legal systems that do not stem from a superior legal order. Unlike Teubner, who has constitutionalized non-state law, Ladeur does not emphasize the "world society" as a source of legitimacy for legitimizing non-state law. Instead, he depicts the law as a heteroarchical phenomenon and fragmented networks. He adds that the non-state legal system functions rationally on the basis of "project-like co-operation and mutual observation" among and between the communities according to their scope. These procedures eventually establish a global "network-society" that is detached from states and far from their interference.[214]

The diversity of social scientific approaches makes it difficult to categorize them. However, according to Tamanaha, social scientific approaches to

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[213] See Gunther Teubner, *Global law without a state* (Aldershot: Dartmouth Publishing, 1997).

[214] Karl-Heinz Ladeur, "The Emergence of the Global Administrative Law and Transnational Regulation" (2011) History and Theory of International Law Series:1 International Law and Justice Working Papers.

law fall into two categories.[215] In the first category, law is observed in the context of "patterns of behaviours."[216] In each society, there are multi-layered social associations like the family, business, and political communities that identify a set of binding rules of conduct in order to normalize their conduct among themselves and with other associations. Ehrlich has called these associations "living law," that is, a set of "customary practices" that regulate the conduct of individuals in the association.[217]

The second category in the social scientific concept of law calls upon an approach similar to states' rules and institutions. According to this approach, law is a norm or custom that has been institutionalized or enforced by official institutions.[218] According to Tamanaha, "Legal norms are only those norms that, when violated, are enforced by publically administered sanctions. All other norms are moral or political or custom or manners or whatever, but not law."[219]

In order to theorize the arbitral legal system, scholars have applied some of these social theories. I am going to introduce two of them.

1. Re-institutionalized customary law

Given that not all social norms and customs deserve to be considered law, conceptualizing law based on norms and customs creates some concerns about

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[215] Tamanaha, *supra* note 206 at 503.

[216] Ibid.

[217] See Eugen Ehrlich, *Fundamental principles of the sociology of law* (New York: Arno Press, 1975).

[218] Tamanaha, *supra* note 206 at 506.

[219] Ibid at 507.

how to distinguish normative order from legal order, what makes them jural, and how norms and customs are transformed to be able to constitute a legal system. In other words, what process should norms and customs go through or what characteristics do they require in order to constitute a legal system? As I pointed out in the previous part, in the legal positivist's approach, a normative order is transformed into a legal system when the secondary rules of recognition, change, and adjudication develop. According to Hart, a legal system is the result of the combination of both primary and secondary rules. Some social theorists, such as Bohannan,[220] have taken a similar approach.

Bohannan uses the idea of "re-institutionalization" or "double institutionalization" to distinguish law from other normative rules. Re-institutionalized customary theory as a social scientific approach seems similar to Hart's primary and secondary rules. Hart's secondary rules of recognition have the same function as re-institutionalized custom does. Both mechanisms restate and recognize the norms and customs that belong to the system. According to Bohannan, only re-institutionalized norms and customs can be considered "law." A norm is defined as a rule that shapes "ought" and "ought-not" in human relationships. Custom, however, is a long-established and consistent practice of those norms that have created an expectation to conform to the behavior accordingly. Bohannan points out that all societies have legal institutions and non-legal institutions "by means of which people of a society settle disputes that arise

[220] Paul Bohannan, *Law and warfare: studies in the anthropology of conflict* (Garden City, N.Y.: Natural History Press, 1967) at 47.

between one another."[221] Customs and norms become law as the result of the practices of these institutions. He continues, "some customs, in some societies, are *reinstitutionalized* at another level: they are restated for the more precise purposes of legal institutions. When this happens, therefore, law may be regarded as a custom that has been restated in order to make it amenable to the activities of the legal institution."[222] These legal institutions must develop a mechanism to deal with difficulties as well; therefore, they create laws about themselves as well as about other institutions in society, such as economic institutions.

Customs, in order to be considered law in a multi-centered society like the international law society, have to be re-institutionalized too, but in a different manner.[223] Now the question is, how does customary law theory, and in particular re-institutionalized custom theory, contribute to theorizing the arbitral legal system? The issue can be viewed from various angles.

First, traditionally, states have an obligation to recognize and follow constant, uniform, generally accepted customs. These customs have been seen as a source of law domestically and internationally. In regard to the growth of non-state actors' indirect participation in shaping international customary law, states are not the only entities dominating the area. This non-state participation, in turn, helps to improve the legitimacy of international customary law.

The definition of customary law should be adjusted according to the circumstances. Non-state actors shape international customary law by

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[221] Ibid at 47.

[222] Ibid.

[223] Ibid at 54.

participating in policymaking processes. They even have replaced state actors in international affairs, and they have obligations and rights in international law. Therefore, international customary law as a source of international law has to be redefined. It is probably justifiable to include international communities' norms and customs as international sources of law. In specific areas, such as international arbitration law, the general acceptance of the community members is sufficient to shape international customary law, and there is no need for a broad acceptance by international communities. [224]

Second, the arbitration society has a series of long-lasting norms and customs that were re-institutionalized and restated in arbitral awards. Arbitral decisions have been restated and applied by arbitral tribunals in various cases. The international arbitration community has also developed a relatively effective mechanism, such as publishing the awards and creating online databases, to systematically recognize and restate these customs. In a very sophisticated form, the international arbitral community has codified these customs in various forms, such as the codification of arbitral rules.

According to Schultz, re-institutionalization of customs occurs in three stages: namely, "the formation of the norm, its application, and its enforcement."[225] By three stages he means that through case law a norm should be recognized and applied; then it has to be forced in practice.

For the purpose of restating norms, there must be (a) relatively independent institution(s) that has/have the power to practice the norms. Under

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[224] Müller, *supra* note 30 at 45.

[225] Schultz, "Private systems" *Supra* note 176 at 174.

this purpose, international commercial arbitration has been recognized as a reliable mechanism and legal institution to settle disputes of the private actors in international business. These institutions have duties, responsibilities, and jurisdiction; and above all, they are expected to formulate arbitral norms and apply them to the case at hand as well as to impose their adjucative power on parties.

2. "Living Law" Theory

One of the most influential theories that have been reflected in the formation of the arbitral legal system is the "living law" observation. Ehrlich, who is known as the founder of the social scientific approach to law,[226] believes that law is a rule or ordering that allocates duties to each member of a social association according to his/her position in the community. The main element of the legal system is, therefore, ordering; as he states:

> It is not an essential element of the concept of law that it be created by the State, nor that it constitute the basis for the decisions of the courts or other tribunals, nor that it be the basis of a legal compulsion consequent upon such a decision. A fourth element remains, and that will have to be the point of departure, i.e. the law is an ordering.[227]

He continues and gives a definition of law as a rule that defines individuals' position and conduct in social associations: "… the law is an organization, that is

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[226] Tamanaha, *supra* note 206 at 503.

[227] Ehrlich, *supra* note 217 at 24.

to say, a rule which assigns to each and every member of the association his position in the community, whether it be of domination or of subjection (*Überordnung*, *Unterordnung*), and his duties.…"[228]

According to Ehrlich, society consists of many social associations, such as family, business, religious, and political communities; and each of them identifies certain binding rules of behavior that members have to follow: "a social association is a plurality of human beings who, in their relations with one another, recognize certain rules of conduct as binding, and, generally at least, actually regulate their conduct according to them."[229] The "inner order" of associations can develop and become the "legal norms." Ehrlich calls these rules "living laws."[230] He suggests that in order to investigate law one "must first concern himself with concrete usages, relation of domination, legal relations, contracts, articles of association, dispositions by last will and testament."[231] Therefore, "The living law is not the part of the content of the document that the courts recognize as binding when they decide a legal controversy, but law is only that part which the parties actually observe as law in life."[232]

As Schultz points out: "Common-sense empirical observations suggest that it is a universal and inevitable phenomenon that norms emerge when a group is formed and remains formed for a certain period of time. Wherever there is a community, there is some sort of ordering, and ordering is inevitably achieved

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[228] Ibid.

[229] Ibid.

[230] Ibid at 34.

[231] Ibid at 501.

[232] Ibid at 497.

through norms."[233]

The point to be observed here is that according to the social scientific theory of law, in order to determine what the law is, one has to investigate by scientific methods the meaning and function of normative order in a specific society. In other words, to determine whether the arbitral normative order deserves to be labeled law, one has to study what is conceived as law in the international arbitral community as a social association.

The international arbitration community as a collective human society has its own laws. Arbitral normative orders are self-organized, self-valued, and include outcome-based rules that have been extracted from legal practice. They emerged and became legitimate by widespread use and confirmation by the international arbitral community.

3) Conclusion

I have found that the reason for the diversification of the concept of law is to address the demands and distinctive needs of societies in different eras with respect to social, political, and technological circumstances. Technological advances, economic developments, and political shifts have influenced the way we conceive of law. Therefore, the concept of law has evolved in all times, i.e. in traditional, modern, and postmodern eras.

It seems to me the law is by nature is a dynamic and evolving process; therefore, all the legal theories that have been mentioned are bound to a specific

[233] Schultz, "Secondary Rules" *Supra* note 143 at 61.

time and are for a specific society. Therefore, they should not be generalized and used in other societies for the purpose of evaluation of the credibility of law.

Therefore, I conclude that "law" has to be constantly redefined for the purpose of including all the phenomena that deserve to be called "legal." Legal theories do not serve as universal panaceas for the past, present, and future. Each society should be studied separately, based on its values, purpose, function, and subjects. In doing so, one should also take into consideration practical reality. Conceptualizing law in the world of pure abstraction is absurd. It seems that social scientific theory of law is more appropriate theory to conceptualize arbitral legal system. It defines "law" in each society based on that society considering its values, purpose, and function and it emancipates law from the states' sovereignty.

CHAPTER THREE
Application of an Autonomous Arbitral Legal System

1) Introduction

In the first chapter, I discussed two main subjects: the factors that impact the transformation of international commercial arbitration from a mechanism of resolution of international commercial disputes to an autonomous legal system, and the signs that point to the existence and validity of the arbitral legal system. The second chapter was dedicated to the theoretical analysis of the arbitral legal system. The legality and systematicity of the arbitral legal system were studied through an exploration of traditional, modern, and postmodern theories of law. In the third chapter, I intend to reflect on the practical consequences of the concept of an autonomous arbitral legal system. The objective of this chapter is therefore a critical review of the application of the arbitral legal system and consideration of its positive and negative impacts on the practice of international commercial arbitration.

The autonomy of international commercial arbitration has had positive impacts on its trusworthy and integrity that in various ways have encouraged states and arbitrators to use such an approach. However, one cannot ignore the practical concerns that an autonomous transnational legal system may generate,

given that the negative practical impacts may cause a legitimacy crisis in a newly emerged arbitral legal system.

2) Necessity of Recognizing the Arbitral Legal System

A. The Arbitral Legal System and the Establishment of Transnational Judicial Justice in the New Global Order

Regarding the current global order, recognition of an autonomous arbitral legal system seems necessary to existing justice beyond the state. Certain degrees of independence for international commercial arbitration will bring about justice internationally by preventing the centralization of power in a few influential states. The autonomy of international commercial arbitration may also puts human rights in a better shape by the distribution of power among all members of the global society, including states and non-governmental entities. Such a transnational private legal system potentially prevents powerful states from monopolizing international commercial arbitration for their own interests. Given that an independent arbitral tribunal can play an intermediary role, it will guarantee the interests of both first-world countries and developing countries by creating a balanced and neutral legal system to resolve international commercial disputes.

Today's global order was established after the Second World War and the collapse of the colonial empires. However, the critical study of the history of the global order suggests that the colonial era has not yet really ended; instead, its

methods and approaches have changed. Some first-world countries that have been using military force to guarantee their profits in developing countries are now pursuing their "neo-colonial" tendencies by modern methods. They and their corporate allies continue to dominate and shape a global order in favor of their own interests.[234]

Up to now, the global society has failed to articulate an alternative global order that reflects all nations' interests. So far, economic policies, international treaties, and commercial legal frameworks have been designed only in some Western cities like Geneva or New York. There is no sign of universal participation.[235] In addition, efforts and movements to ensure practices such as political equality that have been advocated for many years have not been able to solve the injustice and inequality in the international community.[236]

The solution may be found in the recognition of a transnational and trans-systemic private legal system that will shape the global order in different fields. It appears that acknowledging the autonomy of transnational non-state organizations, institutes, and communities can contribute to decolonization movements. Particularly, in the field of international commercial arbitration, the recognition of an autonomous arbitral legal system has the capacity of potentially redistributing power and solving inequalities in international society. This kind of system can contribute to redesigning an international order that will finally limit

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[234] See BS Chimni, "Third World Approaches to International Law: A Manifesto" (2006) 8:1 International Community Law Review.

[235] Ibid.

[236] Mohsen Al Attar & Rosalie Miller, "Towards an Emancipatory International Law: The Bolivarian Reconstruction" (2010) 31:3 Third World Quarterly 347 at 2.

the hegemonic domination of first-world countries in shaping the global order.

In order to be able to cope with the global issues and contemporary challenges, the involvement and cooperation of both state and non-state actors in shaping global norms are needed. It should be borne in mind that most of the time these are non-state entities, such as non-governmental organizations (NGOs), transnational corporations, international institutions, and individual arbitrators who are practicing transnational legal norms.

If they perceive that they have not participated in the creation of those norms, they will have little or no interest in implementing them.[237] Therefore, relying on the state-centered legal order in the field of international commercial arbitration seriously challenges the legitimacy of the arbitral legal system, since the democratic legitimacy of the arbitral legal system in shaping legal orders demands the involvement of all members of the international arbitral community, including non-state actors.[238]

One might argue that the first-world countries and their international academic institutions and the Western-oriented corporations and law firms will inevitably play a key role in influencing the private institutions which try to shape global governance. With their prestige and power, they still have a great deal of influence on arbitration institutions.

To address this concern, we should consider that international commercial arbitration is multi-centric. The recent advancements in international arbitration in the developing states show that all states are actively participating in the

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[237] Müller, *supra* note 30 at 41.

[238] Ibid at 40.

generation of the arbitral decisions. Arbitration centers are emerging in developing countries all over the world, from Latin America to the Middle East and eastern and central Asia. In the current situation, arbitration comprises a plural and multi-polar legal system that is shaped by diverse independent private actors from all over the world and with different backgrounds. Therefore, the international arbitration community can shape a global order that better guarantees justice in the international commercial relations, knowing that international arbitration dynamically evolves, meaning it regularly moves from one place to another and openly interacts with other legal orders. This openness provides the system with the capability of balancing within the system as well as filtering adopted norms in order to prevent intervention and interference by states and transnational corporations.

B. Practical Advantages of Recognition of the Arbitral Legal System

The way that arbitral tribunals see arbitration will have a direct impact on the practical aspects of arbitration. These practical aspects can be studied from different angles. For instance, a proper conception of international commercial arbitration will affect how arbitral tribunals interact with national courts and how they deal with the decisions of the national courts about different aspects of arbitration proceedings. It will also determine which approach arbitrators should take when they are dealing with concepts such as public policy and overriding mandatory rules. It will define the limitations of the arbitrators' power to rule on a

case in the sense that they will have a certain degree of freedom to decide on the arbitration procedure to be used. It will help tribunals to interpret the terms and legal conditions of arbitral contracts and the applicable laws. Given the practical consequences of how arbitrators envisage international commercial arbitration, it seems that an appropriate understanding of arbitration affects the validity of the arbitration process. In my view, from surveying some of the practical consequences of the recognition of the arbitral legal system, it appears that the recognition of an autonomous arbitral legal system is necessary to ensure the credibility of arbitration proceedings.

Neutrality is a crucial quality for a just international dispute-resolution mechanism. To fulfill this quality, arbitral tribunals require a certain independence and autonomy from national legal systems. By such independence, arbitrators will be able to prevent national courts' intervention in arbitration processes.[239] International commercial arbitration and the national legal systems are two completely separate legal systems; therefore, the influence of each is subject to the discretion of the other legal system. Consequently, the conception of an autonomous arbitral legal system allows arbitrators not to follow national courts' decisions unconditionally, particularly, when the decisions are against the arbitral legal system. The benefits of such a concept are revealed when a party attempts through a national court to invalidate an arbitration agreement or the entire arbitral process, or to render an arbitral award ineffective. In this case, the arbitral tribunals should take into account the concept of the arbitral legal system

[239] Gaillard, "L'ordre juridique" *Supra* note 14 at 900.

and ignore the court's decision that conflicts with the nature of international commercial arbitration.[240] A perfidious party can derail the arbitration process by starting various legal actions against arbitration. The arbitral tribunals that conceive of international arbitration as part of the legal system of the seat, take the comparative approach to international arbitration, or believe that arbitration is connected to the several national legal systems will have to obey the court's decision. Otherwise, they put the arbitral award at risk of being annulled or not being recognized by the national legal systems. In all cases, whether the tribunal applies the court's decision or denies it, the arbitration process will be negatively affected by hostile injunctions.[241]

The solution is a change of approach and the conceptualization of arbitration as an independent transnational legal system. In this case, the arbitral tribunals have to assess national courts' decisions against universally accepted arbitral rules.

Arbitral tribunals face the same problem when dealing with the application of national mandatory rules. The arbitral tribunals that are aware of their transnational role should also be reluctant to put into effect the mandatory rules of the country of the seat or the applicable law, where those are not compatible with the arbitral legal system. Gaillard gives the example of ICC case number 6397 in 1990, in which an arbitral tribunal rejected applying the mandatory rules of a state with the justification that the arbitral tribunal is not part of the domestic legal

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[240] Ibid.

[241] Ibid.

order.[242] Acknowledgment of the autonomous arbitral legal system demands a new approach to national mandatory rules, an approach that limits the effect of those rules on the arbitration.

The next positive practical impact of the notion of the arbitral legal system in the operation of the arbitration is procedural flexibility. Whereas classical courts rule on a case according to the rigid rules of law, international commercial arbitration has a flexible procedure. Arbitrators should be able to benefit from diverse resolution methods in order to resolve disputes. The flexibility of the arbitration process is one of the reasons that have made arbitration attractive for the international commercial activists. Ralf Michaels explains some of the methodological differences between the national courts and arbitration:

> Where state law relied on formalistic and abstract legal rules, arbitration offered the attraction of decisions based on equity, tailored to the specific requirements, unbound by a system of binding statute or precedent. Where state courts relied on legal experts with little expertise on the specific requirements of commerce, arbitrators were themselves merchants who knew about such requirements.[243]

The notion of the arbitral legal system enhances arbitrators' power to adjudicate cases in a way that reflects the methods that have been fostered by merchants over many years. The flexibility of the dispute-resolution mechanism is indeed a crucial factor to foster international business and serve the arbitration

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[242] Ibid at 902-903. ICC Case no 6379 (1990), (1996) 7:1 ICC International Court of Arbitration Bulletin 83, at 85.

[243] Michaels, *supra* note 155 at 455.

users in a more appropriate manner. It also allows arbitrators to rule on arbitral cases according to the specific needs of a particular business community and to freely tailor a proceeding that fits better with the parties' needs and objectives.

Finally, the concept of the arbitral legal system makes it possible for arbitrators and national courts to interpret fairly the terms and concepts in documents, arbitration agreements, and procedural and substantive law. A fair interpretation is not possible without consideration of the arbitration legal system as a whole. Understanding a fact or legal rule in a legal system should not occur in isolation, because this would not lead to a solution that is coordinated with the whole system. Bobbio calls the isolationist approach "looking at the tree instead of the forest."[244] In order to interpret the legal norms and legal concepts in international commercial arbitration, arbitrators have to take into account the totality of arbitration, its entire rationality, and its ultimate objectives and purposes. Therefore, it is the duty of arbitrators in the interpretation process to strike a balance between opposite poles, i.e. their freedom and subjectivity with consideration of the conditions of the case in hand, from one side, and generally accepted arbitral rules in the international arbitration community, on the other side.

The interpretation of public policy in international commercial arbitration is a good example. Arbitrators have developed a new concept and embrace the notion of transnational public policy in dealing with public policy issues in international commercial arbitration. Arbitral tribunals have basically adopted a

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[244] Norberto Bobbio, *Teoriadell' ordinamento giuridico* (Turin: Giapprichelli, 1960), Van De Krechove & Ost, *Supra* note 15 at 2.

narrower definition of public policy as it applies to international cases as opposed to a broader definition of public policy in domestic matters.[245] Gaillard explains that in the practice of international commercial arbitration, arbitrators as guarantors of the arbitral legal system choose "transnational public policy" or "true public policy" over domestic public policy.[246] The emergence of this notion is the result of the consideration of the general rationality of arbitration and the objective of arbitration as an independent legal system. This interpretation has resulted in the transformation of an old notion and the adoption of a new concept that is compatible with the arbitral legal system as a whole.

3) Critical Review of the Application of the Arbitral Legal System

Besides the positive impacts of the application of the arbitral legal system on the validity and credibility of international commercial arbitration, there are also some serious practical concerns about the application of the arbitral legal system.

The first concern arises from the contractual nature of arbitration. The contractual nature of arbitration generates a difficulty in extending parties' agreement to arbitrate to the arbitral legal system, particularly when there is no

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[245] For more information regarding the notion of "transnational public policy"and its distinction from domestic public policy, see the second chapter and the discussion about the limitation of states' intervention in arbitration processes. Van den Berg, "Distinction Domestic-International Public Policy" in Van den Berg, ed, *Yearbook Commercial Arbitration, Consolidated Commentary of Cases Reported in Volumes XXI* (Internnational Counsil for Commercial Arbitration, 1996) 394-520 at 502. Online: <http://www.kluwerarbitration.com/book-toc.aspx?book=TOC_ICCAYB_1996_V02>

[246] Gaillard, "L'ordre juridique" *supra* note 14 at 902-903.

social reflexivity in the arbitral legal system. In other words, when parties do not normally participate in shaping the arbitral legal system, it is difficult to generalize an arbitration agreement to the arbitral legal system. The other concern relates to protection of public interests. In this respect, the main question is whether or not a private a-national legal system is capable of protecting public interests. The last concern is the practical issues that arise from the co-existence of different competing legal systems. These practical difficulties will be discussed in the following parts.

A. Dealing with the principle of party autonomy

International commercial arbitration is contractual by nature. Parties submit their disputes to arbitration by consent. They determine the legal framework of the arbitration, including the formation of the tribunal, the arbitrator's duties and limitations, applicable laws, and even the termination of the arbitration. Arbitrators are bound to the conditions and limitations in the arbitration agreement. They have to assess their decisions and orders with consideration of the explicit and implicit consent of the parties. Furthermore, given that the main purpose of arbitration is resolving disputes between parties, arbitrators should encourage both parties to participate in all decision-making processes. Participation will indeed increase the possibility of the voluntary performance of the award and will fulfill the main objective of the arbitration, which is to resolve the legal issues.

On the other hand, relying on the theory of the autonomous arbitral legal

system, arbitrators have to follow the arbitral legal system and the arbitral precedents that have been emerging in the international arbitration community. In other words, the concept of the arbitral legal system imposes a duty on arbitral tribunals to rule on a case on the basis of its own recognizable rules. A problem arises when the principle of party autonomy is in conflict with the concept of the arbitral legal system. The parties may explicitly consent not to consider international commercial arbitration as an independent legal system and request the arbitrators not to consider the arbitral precedents. It can also be inferred that parties do not consent to the consideration of the arbitral legal system by choosing a national law as the only applicable law, or by agreeing on a rule that contradicts arbitral legal system.

Given the importance of party autonomy in the arbitration process, it seems that the arbitrators have to respect the explicit and implicit consent of the parties up to the point that there is no contradiction with the essential characteristics of the arbitral legal system that would challenge the validity of the whole process. One example may clarify this. It is a well-established practice that arbitrators should be independent and impartial. The International Bar Association Guidelines on Conflicts of Interest in International Arbitration (IBA Guidelines)[247] set a comprehensive list of the relationships that may lead to partiality and dependency and conflicts of interest. According to the IBA Guidelines, arbitrators are under a duty to disclose any conflicts of interest or

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[247] IBA Guidelines on Conflicts of Interest in International Arbitration (2004) online: <http://www.ibanet.org/ENews_Archive/IBA_July_2008_ENews_ArbitrationMultipleLang.aspx>

factors that might affect their integrity. The Guidelines also set a "Red List" specifying situations that if one which should occur, an arbitrator should refuse to serve. The "Red List" has two sections: waivable and non-waivable relationships. Parties may waive the impartiality or independency condition of the arbitrator if the relationship is listed in the waivable part of the "Red List" and any agreement to waive the non-waivable relationship is considered invalid.[248] From studying the "Non-waivable Red List"of the IBA Guidelines,[249] it seems that the main reason for not permitting parties to waive a relationship is that it endangers the integrity of the entire arbitration process because it is contrary to the entire nature of international commercial arbitration. Therefore, the Guidelines have limited party autonomy in favor of the credibility of the arbitration process.[250]

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[248] The IBA General Standard in the section (4) about the waiver by parties states:

"(C) A person should not serve as an arbitrator when a conflict of interest, such as those exemplified in the waivable Red List, exists. Nevertheless, such a person may accept appointment as arbitrator or continue to act as an arbitrator, if the following conditions are met:

(i) All parties, all arbitrators and the arbitration institution or other appointing authority (if any) must have full knowledge of the conflict of interest; and

(ii) All parties must expressly agree that such person may serve as arbitrator despite the conflict of interest."

[249] IBA Guidelines: "1. Non-Waivable Red List:

1.1. There is an identity between a party and the arbitrator, or the arbitrator is a legal representative of an entity that is a party in the arbitration.

1.2. The arbitrator is a manager, director or member of the supervisory board, or has a similar controlling influence in one of the parties.

1.3. The arbitrator has a significant financial interest in one of the parties or the outcome of the case.

1.4. The arbitrator regularly advises the appointing party or an affiliate of the appointing party, and the arbitrator or his or her firm derives a significant financial income therefrom."

[250] See William W Park, "Arbitrator integrity: the transient and the permanent"(2009) 46:3 San Diego L Rev 629 at 638-638.

The next question relates to the situation in which parties agree on the arbitration without any explicit or implicit consent on the arbitral legal system. The problem is whether or not the parties' consent to arbitrate can be considered as permission to decide on their cases on the basis of the arbitral legal system.

The problem becomes more obvious when it is considered that the parties are not part of the process that produces the arbitral legal system. The arbitral legal system has been criticized because they do not have the social-reflexivity condition that is essential for a democratic legal system. In a classic legal system, participation of the subject of the legal order in generating the legal order' processes is considered essential; otherwise, when parties are absent from the process, the legalization process would not be democratic.[251]

The arbitral legal system is not an exception. The legitimacy of the arbitral legal system depends on this notion of whether it represents the will of the whole international arbitration community. Therefore, it requires the circulation of the information among the members of the entire community. With respect to reflexivity, the arbitral legal system has been criticized in two ways. First, it seems that merchants are being excluded from the legalization process, because the arbitral legal system inasmuch as it consists of arbitral decision, is created by arbitrators, not merchants themselves. Second, given the transparency issue in the decision-making process and publication of the arbitral awards in international commercial arbitration, it is very difficult to say whether the parties are even

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[251] See Gralf-Peter Calliess, "Lex Mercatoria: A Reflexive Law Guide to an Autonomous Legal System", online: (2001) German Law Journal <http://www.germanlawjournal.com/article.php?id=109>.

aware of such a legal system.

One answer to the criticisms is to argue that international business communities participate indirectly in the genesis of the arbitral desicions. Arbitration cases are decided on the basis of the rules of law and general principles that have emerged in the international business communities over many years. These practices and trade usages have been recognized and constitutionalized by the arbitral tribunals.

In addition, it seems that parties' agreement to arbitrate can be interpreted as their consent to the arbitral legal system as well, because the concept of the arbitral legal system serves the arbitration users according to the parties' expectations. The parties in international commercial arbitration expect to submit their disputes to a legal system that can guarantee fairness and efficiency. From my point of view, the concept of an arbitral legal system provides a fair arbitration process for the following reasons. First, it is a trans-systemic and transnational legal system that fits better within the international nature of arbitration. Second, it helps to provide the commercial communities with unified and predictable legal rules in order to treat like cases alike.

B. Coexistence of competing legal systems

Establishing an appropriate relationship between the state and non-state legal systems that govern international commercial arbitration is one of the most complicated dilemmas. The coexistence of several competing legal systems to govern international arbitration results in a lack of coordination in the

proceedings of international arbitration.

Universality and a tendency towards expansion are aspects of legal systems' nature. They originated from their normative activities to bind their subjects.[252] Each legal system has to determine its relationship with other existing legal systems. Legal systems' tolerance in acceptance of other systems is different.[253] Basically, the diversity in legal systems' approaches is due to how they conceive law and how they "reconcile their normativity with their own tolerance."[254]

The conflict of national legal systems with the arbitral legal system has a negative impact on the practice of arbitration. It damages the operation of justice in the long term by creating practical obstacles.

Conflicts between national legal systems and the arbitral legal system appear in several forms. Among them, I would like to discuss the intervention of national courts in international arbitration and the relative recognition of the arbitral legal system. In both forms, the conflicts reveal some practical issues that may seriously affect the fairness and efficiency of international commercial arbitration.

Competition between legal systems for dominance in the legal field prevents the realization of the true mandate of a legal system, which is fulfillment of justice. Without the reconciliation of legal systems, emerging innovative legal solutions will face failure. According to Professor Glenn's theory of "reconciling

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[252] H Patrick Glenn, *Legal traditions of the world: sustainable diversity in law* (Oxford: Oxford University Press, 2010) at 365.

[253] Ibid.

[254] Ibid.

legal traditions," it seems necessary to accept and recognize existing legal traditions to accomplish "the legal mission."[255]

1. Public policy and states' intervention in arbitration proceedings

The conflict between two independent legal systems happens when a national court intervenes in the arbitration process to review the validity of an arbitral agreement, the fairness of international commercial arbitration, of the possibility of the violation of a state's public policy.

On one side, there is no legitimate ground for states to interfere in an autonomous and independent legal system.[256] The existence of a legal system that governs one area prevents other legal systems from intervening.

An analogous relationship can be found in international relationships and among states where the independence of a state's legal system is a well-established principle and states based on the territoriality principle are prohibited from interfering with others' legal affairs. Similarly, the concept of the arbitral legal system demands that states take a non-interference approach or adopt a *laissez-faire* policy towards international commercial arbitration.

On the other side, the globe is divided into states where every legal activity occurs within a single state's territory and where the states do not want to give up their sovereignty. Even if they recognize a private mechanism to settle business disputes, the authorization is not unconditional. States reserve for

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[255] Ibid at 377-378.

[256] Mustill, supra note 161 at 117; Schultz, "Concept of Law" *Supra* note 170.

themselves a right to review and supervise arbitration because of their mistrust of a private legal system.

The commercial sectors by nature are mostly concerned about their commercial activities and profits. In the field of business, the priority is to develop business and survive intense international competition. This is not going to happen without concentration on the demands of the market and institutions' profits. For this reason, the legal order that emerges from the international arbitration community, unsurprisingly, would take a utilitarian approach and be consistent with the protection of the main objective of the market. This gives rise to concern over other functions of a legal system, such as protection of public policy, human rights, long-term and strategic economic measures, universal moral values, and so on.

Similarly, the concept of the arbitral legal system creates concern about whether or how such a private legal system could protect public policy. This concern seems to be justifiable given that the arbitral legal system neither has the capacity to develop nor an instrument to impose measures to protect public policy. There is also a serious concern about abuse of the independent arbitral legal system in favor of the economic interests of certain powerful international corporations.[257] This also generates uncertainty about the arbitral legal system's capability to make itself immune to being influenced by giant international corporations and their hegemonic tendencies.

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[257] Stephen J Toope, *Mixed international arbitration: studies in arbitration between states and private persons* (Cambridge: Research Centre for International Law of the University of Cambridge, 1990) at 96.

In addition, the incapability and lack of required instruments of anational rules to defend public order has probably convinced some scholars to deny the existence of any such legal system. They also suppose that governments are the only source of political power to defend the fundamental economic, social, and political rules, thereby giving the right to states to supervise arbitral processes and awards.

Mistrust of anational rules is not a recent issue. It made the majority of positivists think that a-national law is factious or unthinkable. The early legal positivists, like Hobbes, Bentham, Kelsen, and Austin, observed the issue and concluded that law is subject to political sovereignty and that there must be a connection between the concept of law and sovereignty. There are strong voices from dominant legal theorists that claim that "there is no other justice than the justice to be found in the positive law of states."[258] Or "There is no guarantee for justice outside the government."[259] The perception of law or legal rules has been deemed widely connected to imperative orders rendered by a sovereign state. States are supposed to predict societies' short- and long-term main interests and, therefore, are able to create a balance between private and public interests. Governments are assumed to be the only source to protect the fundamental rights of a society as a whole against the advantage of a small part of the society.

Although the majority of states reserve a right to review arbitral processes and awards, the quality of this kind review is varied and depends on how they

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[258] Schultz, "Concept of Law" *Supra* note 170 at 62.

[259] Santos Boaventura de Sousa, *Toward a new legal common sense, law, globalization, and emancipation* (London: Butterworths LexisNexis, 2002) at 90.

conceive arbitration. The adoption of the concept of arbitral legal justice suggests taking a non-intervening approach, while denying the existence of an arbitral legal system gives absolute right to states to execute a full-review of arbitration processes. Therefore, the adoption of different theories leads states to take extreme approaches. As experience has proved, too much or too little interference is not constructive.[260] In order to develop a constructive relationship, a moderate system of judicial review must be applied that considers the autonomy of the arbitral legal system and, at the same time, gives a limited power to the courts for judicial review in order to protect public policy.

2. Finality of Arbitral Awards and Relative Recognition of the Arbitral Legal System

Diverse approaches of national courts towards international arbitration and adoption of various legal theories by national legal systems have created challenges for international arbitration. This has been to such an extent that some states, like France, have taken a liberal approach with a tendency to embrace the arbitral legal system theory, whereas other states have taken a more conservative approach that considers international commercial arbitration as part of the legal system of the seat. Therefore, the arbitral legal system is a phenomenon that is interpreted differently from one jurisdiction to another. It is recognized by some states, while other jurisdictions deny its existence. This lack of coordination across the legal systems has in turn created uncertainty in the arbitration process

[260] See Abedian, *supra* note 63.

because the possibility always exists of national courts making conflicting decisions over a similar case.

Recognition of the arbitral legal system by states is similar to the recognition of a state that has seceded by other sovereign states. "One state may recognize the independence of the seceded part of a state and its laws while other states refuse to do so and only acknowledge the law of the mother state."[261] Schultz has called the situation in which a national legal system perceives a "non-state normative order" as law while others deny it "relative legality."[262]

The relative legality of the arbitral legal system has caused some practical difficulties. For instance, the discrepancy of states' approaches to international commercial arbitration could challenge the finality of arbitral awards. Given that annulment of an arbitral award by a state does not affect the validity of the award, this situation, therefore, gives rise to the possibility of recognition of an arbitral award that had been annulled abroad.

There are no serious grounds to prevent other jurisdictions from recognizing and enforcing of an annulled award. Some scholars have argued that state courts should refuse the recognition of such an award under the principle of international comity. According to that principle, states should recognize the judicial acts of another state to the greatest extent in order to foster mutual respect and facilitate inter-jurisdictional relationships.[263] It seems, however, that such a political consideration will not prevent national courts from hearing the case

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[261] Schultz, "Secondary Rules" *Supra* note 143 at 84.

[262] Ibid.

[263] Ibid at 85.

because international comity is a non-binding practice. Furthermore, if a national court refuses to recognize an award based on the fact that it has been annulled in a foreign country, the party may be considered as "being denied access to justice."[264]

It seems that the concept of an arbitral legal system will negatively impact the finality of arbitral awards and that it is justifiable on the basis of the transnational nature of international commercial arbitration. As Shultz states, "the quality of justice of arbitration often exceeds the quality of justice of the national legal system that has annulled the award."[265]

In my view, the solution may be found in Professor Glenn's theory of reconciling legal traditions. [266] According to that theory, there exist various legal traditions in the world, including known legal traditions and unidentified legal traditions that are waiting to be recognized or investigated. Normativity is a common feature of legal traditions; and therefore, they have a tendency to expand their domain towards "universality". It is thus an inevitable challenge for legal traditions to deal with the conflicts emerging from and the "incommensurability" with other legal traditions. As Professor Glenn suggests, universalizing a legal tradition depends on "how it reconciles its own normativity with its own tolerance of other traditions."[267] According to him, "there is a sustainable diversity in law in

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[264] Ibid at 104.

[265] Ibid at 86.

[266] See Glenn *supra* note 252.

[267] Ibid at 365.

the world"[268] ; and going against this trend will result in damage. Any attempt of the major legal traditions to dominate will overshadow the changes and innovations that smaller or younger legal traditions may bring about. In contrast, working within a framework of diverse legal traditions will improve the peaceful settlement of disputes. The theory of reconciling legal traditions suggests solving conflicts between legal traditions by finding a "middle ground."To do so, legal traditions need to identify and recognize other legal traditions. Particularly, knowing more about "the source of alleged incommensurability"[269] will aid reconciliation of legal traditions.

[268] Ibid at 377.

[269] Ibid at 379.

GENERAL CONCLUSION

As I discussed in the first chapter, globalization has played a key role in the creation of the arbitral legal system. As a result of the globalized economy, the use of international arbitration has expanded. International arbitration has received particular attention from international merchants as a means to settle their disputes because arbitration does not have the limitations that national courts are dealing with in the context of international cases. Arbitration is superior to other mechanisms of resolution of international commercial disputes since it has overcome the practical obstacles of the old solutions, such as choice of law and choice of court. Being neutral, impartial, binding, and flexible and having a trans-national legal framework have made arbitration the most suitable mechanism in international cases. Arbitration, therefore, in order to answer the new demands of arbitration users and developments of the market, has been institutionalized. The institutionalization of arbitration has made it possible to systematically collect and publish arbitration awards. Accessibility to the arbitral awards, in turn, brings awareness among scholars, and it can initiate interactions among the international arbitration community that will eventually increase the legal certainty and predictability of arbitration.

Emerging arbitration institutions have coincided with the increase in the role of private actors and the limitation of states' sovereignty in global governance. The qualitative and quantitative growth of non-governmental organizations, transnational companies, and international institutions has

developed private actors' capacity of making policies and standards for their own activities. Therefore, new norms and standards outside governments have been created. States also have been forced to recognize the influential role of private actors in global ordering and to adopt a liberal approach towards them.

The process of power shifting has affected how international commercial arbitration is conceived and conceptualized. The globalized economy has increased the pace of transition of arbitration from an elementary to a more advanced state. At the embryonic stage, arbitration was a mere mechanism to resolve international commercial disputes within a national legal system. In the early stages, it gained more independence from national legal systems and became decentralized through the application of transnational rules of law, such as the *lex mercatoria* and general legal principles. Finally, arbitration has entered its mature state and has been systemized, thereby generating its own legal rules.

Arbitration has been transformed into a rationalized and systemized legal order. Intense interactions among and between merchants, arbitrators, lawyers, and scholars have created the international arbitration community. These interactions and the exchange of ideas have turned into sophisticated networks through which different ideas get reconciled and balanced. The competition of among the international arbitration communitt to create a more just arbitral process has legitimized international arbitration. In addition, the institutionalization of arbitration has boosted its systematicity and systematization. In order to cope with inequalities of power distributed across the users of arbitration, the international arbitral community has attempted to create a

transnational legal framework that is neutral and independent from national legal systems.

The detachment and independence of international commercial arbitration from national legal systems have been reflected in international treaties, national statutes, and courts' decisions. As I discussed in the first chapter, the discretion that the New York Convention has granted to a contracting state to recognize an award that has been annulled in the country of origin is a sign that signals the awareness of the international community about the specificity of the source of validity of international arbitration. The transnational source of international arbitration has been reflected in courts' decisions as well. In the Hilmarton case the French courts recognized the awards that had been annulled in the country of origin on the ground that arbitral awards are not integrated into the national legal system of the seat. In the Putrabali case, the court went beyond that and argued that arbitral awards are part of international justice; and therefore, the validity of arbitral awards is not derived from national legal systems.

States have affirmed the autonomy of arbitration in various forms. The emergence of new terminologies and the creation of new judicial opinions are indications of states' tendency towards acknowledging the existence of the arbitral legal system. For instance, national legal systems have accepted the notion of transnational public policy and have adopted a narrower definition of public policy when dealing with international arbitration. The recognition of the arbitral legal system has also been reflected in the harmonization and modernization of the arbitration rules in national legal systems. Legislation regarding international commercial arbitration has been inspired by practice. In the harmonization

process, most states have adopted the Model Law. The Model Law, according to its preamble, is inspired by the practice of arbitration and the needs of arbitration users. Therefore, the adoption of the Model Law indirectly confirms the validity of the arbitral legal system. The experience of the harmonization of arbitration rules has led some states to take a more liberal, non-interference approach to international arbitration. For instance, in some jurisdictions, legislators and courts have applied the mandatory and voluntary elimination of judicial review in some arbitral cases. Some states' taking a *laissez-faire* approach has demonstrated a tendency on the part of states to recognize the autonomous arbitral legal system. Finally, states are increasingly allowing parties to choose non-state substantive rules as applicable law. Codified legal principles, guidelines, model contracts, standard terms, model laws, trade usages and customs, and the *lex mercatoria* are playing very important roles in the negotiation, contract drafting, and conflict resolution processes. The sources of national and transnational arbitration procedural and substantive laws are interconnected. Therefore, referring to each set of rules—national or transnational—has produced relatively the same legal consequences.

In the second chapter, I analyzed the theoretical grounds for the legality and systematicity of the arbitral legal system. At the end of that chapter, I arrived at the conclusion that law is a dynamic phenomenon; and in order to define it, one has to consider all the circumstances and specific needs of a specific time. Regarding the legality of the arbitral legal system, the concept of law has been undergoing a process of transformation throughout history. In the evolutionary course of the concept of law, different aspects, such as social and political

conditions, economic shifts, scientific progress, and the globalization process have caused alterations in the approaches to the study of law. As I discussed, the study of law has gone through three different stages.

In the first stage, the study of law was philosophical and distanced from the practice of law. During that period, most theorists adopted natural law. According to the theory of natural law, the source of law is a set of universal moral standards. These standards evolve and are translated into an efficient method in order to put them into daily practice. In the modern era, natural law has continued to influence legal practices and theories. For instance, in violation of human rights cases, international courts have applied the "universal principle of human dignity" to determine war criminals' responsibility. Natural law has also inspired some scholars to theorize about the arbitral legal system. According to naturalists, by choosing a flexible legal framework like arbitration, parties authorize arbitrators to proceed to arbitration based on fairness, friendly agreements, and the commercial needs of the arbitration users. In addition, in several arbitration cases, arbitrators have mentioned general principles of law, universal moral principles and standards, and ethical values as the source of their reasoning. They have used them as sources of law, means of interpretation of national laws, and indicators for assessment of the applicability of national laws in international cases. Despite the influence of natural law theory in theorizing the arbitral legal system, the theory generates some theoretical and practical difficulties. For instance, given the diversity of legal traditions, it seems inaccurate to envisage a set of "universal" moral values. Furthermore, application of moral values in arbitration cases generates legal uncertainty and

unpredictability because the perception of moral values is a personal experience and subject to arbitrators' conscience. Therefore, there is no indisputable method available to assess the credibility of morally right acts and moral principles.

As a result of socio-political changes, modernism, and the redefinition of the relationship between individuals' rights and sovereign states, "law" became the product of sovereign and democratic institutions. Furthermore, through the growth of legal practices, "law" became the product of legal practices. In this period, the jurisprudential approach to the study of law emerged and legal positivism became the dominant legal theory. The temporal and geographic diversity of legal positivism makes it difficult to define. Legal positivism has been interpreted differently. I have arranged the variations of legal positivism into three categories in order to facilitate studying them. The three categories are traditional, modern, and postmodern positivism.

According to transnational positivists, the non-state normative systems turn into a transnational system of arbitral rules by being systematically referred to in international arbitration procedures, considering that the legality of such a system depends on the recognition of states. Opponents of the notion of an arbitral legal system basically argue that recognition of the autonomy of arbitration by some states does not suffice for arbitration to be considered an independent legal system. They conclude that the legality and systematicity of arbitral rules should be assessed on the basis of arbitration's characteristics. Given that the theory of transnational positivism contains some contextual contradictions and does not perfectly match the legal positivists' concept of law, arbitrators and scholars have applied legal positivists' insights in order to assess the validity of the arbitral legal

system.

The arbitral legal system has been criticized by appealing to Hart's secondary rules of law. Secondary rules of law have been interpreted as a set of "social conventions" among those who officially practice law. After a certain period of time, the social conventions evolved into the binding customs that would be considered by members of the society as law. Critics argue that the arbitral legal system has several defects in both primary and secondary rules; therefore, it does not deserve to be considered an autonomous legal system. Despite theoretical controversies and given the issue of practical importance, I have taken a position that advocates that the *lex mercatoria* can be an a-national reliable source in the practice of arbitration.

In addition, lack of transparency in arbitration processes has been seen as a serious obstacle to the systematicity and systematization of arbitration. The transparency and legality of the arbitral legal system have been assessed by using Fuller's theory of an "inner morality of law." Arbitration is outcome-centered modes of making rules. Therefore, the criticism is that they suffer from procedural deficiencies such as lack of "generality," "steadiness," and "public ascertainability" that prevent them from evolving into an independent legal system. Deficiencies in the publication of international commercial arbitral awards, generation of precedents, and mechanisms to unify the arbitral awards prevent arbitration from being systematized. The transformation and development of a normative order into a legal system occurs gradually. Since elementary legal systems constantly develop into more sophisticated ones, a dogmatic theory of

law does not fit international arbitration because the arbitral legal system is a relatively new legal system.

The systematicity of arbitration has been also criticized by invoking the Fullerian "inner morality of law" theory. Scholars have applied Fuller's eight procedural principles to assess whether arbitration acquires the formal qualifications to be considered a just legal system. I have concluded that there are two basic reasons that make these assessments of rules of law unjustifiable. First, Fuller's procedural criteria of law are about legislation, while the arbitral legal system is essentially case-based law. Secondly, the focal point to assess the credibility of a legal system in a case law system, like that of arbitration, is the rationality and reasoning of case law. Application of certain moral criteria to determine the legality of arbitral system does not properly belong to the nature of international arbitration.

According to both the Fullerian and Hartian legal theories, lack of transparency in international commercial arbitration has been considered a serious obstacle to the systemization of the arbitral legal system. Given that transparency is directly correlated with the precedential power of arbitral awards, it follows that issues of confidentiality, the low rate of publication of arbitral awards, and their having an ad hoc basis prevent international commercial arbitration from creating widely acknowledged precedents. Arbitral awards are, allegedly, "situation-specific directives" that cannot be generalized to other cases, nor are they capable of generating general guidelines to be followed in other arbitral cases.

Given the non-hierarchical nature of the arbitral legal system, the idea of precedent in arbitration has a different definition and function compared to the

same idea in national legal systems. The precedential power of arbitral awards is due to their persuasiveness and strength of reasoning. From examining the quality of the published awards, I have concluded that the current publication rate is sufficient to be considered as the representatives of the arbitral decisions.

Because arbitral legal system cannot be theorized only on the basis of morality or states' activities, some arbitrators have taken a social scientific approach to conceptualizing arbitral legal system. On this view, in order to conceptualize law, one must scrutinize human interactions in a specific society. As I have pointed out, as a result of the autonomy that social scientific approaches grant to the concept of law, they have attracted scholars in theorizing transnational law. Among the social theories of law, "living law" and "re-institutionalized customary law" have received most attention. The international arbitration community has developed series of norms, customs, and orders that have emerged and become legitimate through wide use and confirmation. In addition, these series of long-lasting norms and customs in the international arbitration community have transformed it from a set of norm into an autonomous legal system by re-institutionalization and re-statement in the arbitral awards.

By historical analysis of various legal theories, given the dynamicity and evolving nature of law, I have concluded that there is no general definition of law. Therefore, law should be studied in a specific society or community, based on what is conceived as a binding law by that society's members. In doing so, one should also take into consideration the society's values, purpose, function, and subjects as well as practical realities. Therefore, analyzing the legality and

systematicity of the arbitral legal system merely by traditional and modern legal theories will not produce a satisfactory result.

It seems that a dogmatic theory of law does not fit the reality of international arbitration. The arbitral legal system as a relatively newly emerged legal system will have to go through a number of stages in order to become a perfectly transparent, consistent, and predictable legal system.

In the last chapter, I critically reviewed the application of the arbitral legal system and considered its positive and negative impacts on the practice of international commercial arbitration. I conclude that the establishment of transnational justice in the new global order demands adherence to the concept of an arbitral legal system. It helps to prevent the centralization of power in a few influential states and aids in distributing power among all members of the global society.

The practical advantages of the recognition of the arbitral legal system are significant. It is necessary to the credibility of arbitration proceedings in several ways. The autonomous arbitral system enhances the neutrality of the arbitral tribunals by preventing national legal systems from inappropriate interference in the arbitration process. It also maintains the flexibility of international commercial arbitration by giving more power to arbitrators to adjudicate arbitral cases following methods that have been fostered by merchants. It permits arbitrators to rule on arbitral cases according to the specific needs of a particular business community and to freely decide on a proceeding that better serves business communities according to the parties' needs and objectives.

Recognition of the arbitral legal system can also have negative impacts on

the practice of arbitration. Given the contractual nature of arbitration, the arbitral legal system may contest parties' autonomy. Because parties do not normally participate in the shaping of the arbitral legal system, generalizing arbitration agreements to the arbitral legal system seems problematic. However, it appears that international business activists do participate in the genesis of arbitral norms indirectly, since it is known that arbitration cases are solved on the basis of rules that have been fostered by business practitioners. In addition, it is a challenging task for arbitrators to solve possible contradictions between parties' agreements and the arbitral legal system. I also conclude that arbitral tribunals should respect party autonomy up to the point that it does not endanger the integrity of the entire arbitration process and to the degree that it is not contrary to the nature of international commercial arbitration.

The other practical challenge relates to the lack of coordination in the proceedings of international arbitration resulting from the coexistence of several legal systems that are competing to dominate international commercial arbitration. The competition of legal systems in the field of international arbitration may result, for instance, in too much intervention by national legal systems in arbitration processes. It also could endanger the finality of arbitral awards. The solution should be sought in fostering a cooperative atmosphere instead of a competitive environment. As Professor Glenn suggests, legal traditions should be accepted and reconciled rather than denied.

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