State Contracts in Contemporary International Law: Monist versus Dualist Controversies

A.F.M. Maniruzzaman*

Abstract

The theory of internationalization of state contracts poses some of the hardest questions that relate to both public and private international law. The theory suggests that, no matter what law the parties to such a contract choose as the proper law of the contract, international law superimposes their choice and applies automatically as the overriding governing law. Thus where the law of the host state applies as the sole applicable law either by virtue of the parties' express choice or by the conflict of laws rule of closest connection in the absence of such choice, the theory of internationalization triggers off not only the theoretical controversies of monism versus dualism of public international law but also the issues of party autonomy and the doctrine of the proper law of the contract in private international law. Besides theoretical interest, the matter has great practical importance in the real world of foreign investment dispute settlement. While critically examining these issues in the context of international commercial arbitration, the article also looks at other relevant issues such as the authority of private international arbitral tribunals to deal with public international law remedies for breach of state contracts.

Recently, there seems to be a trend to provide expressly the law of the host state as the proper law or applicable law in international 'economic development agreements' (EDAs)[1] between a host state or a state enterprise, on the one hand, and a foreign investor or a multinational corporation on the other.[2] Such a tendency with

* Ph.D. (Cambridge); Lecturer in Law, University of Kent at Canterbury. UK Advocate, Supreme Court of Bangladesh.

1 In the present article, the expressions 'economic development agreement', 'state contract', 'international investment agreement' and 'foreign investment agreement' have been used interchangeably.

2 See, for example, Bangladeshi Model Production Sharing Contract (March 1997), Article 28(1) ('Applicable law'): 'The validity, interpretation and implementation of the Contract shall be governed by the law of the People's Republic of Bangladesh.' See Martin Bartels, *Contractual Adaptation and Conflict Resolution* (1985) 107; Juha Kuusi, *The Host State and the Transnational Corporation* (1979) 145; Delaume, 'The Proper Law of State Contracts and the Lex Mercatoria: A Reappraisal', 3 *ICSID Rev-FILJ* (1988) 79, at 79–81; Delaume, 'The Proper Law of State Contracts Revisited', 12 *ICSID Rev-FILJ* (1997) 1, at 1–28.

EJIL (2001), Vol. 12 No. 2, 309–328

the Third World developing countries seems to be increasingly acute as a reflection of the menace of oft-idiosyncratic arbitral approaches to the choice-of-law issue.[3] Many developed countries are also often found to insist on the application of their own national law to natural resource development agreements.[4] From their vantage point — that performance of such international contracts takes place in the territory of the host state — the host states consider themselves well placed to assume that it allows them to insist that the application of their own law is desirable and practical in day-to-day operations. The law of a state may sometimes mandatorily require it to contract by reference to its own national law.[5] The exclusive role of such chosen host state law has been beclouded by the most controversial theory of internationalization of EDAs or state contracts. Thus, obviously in the context of the theory of internationalization, the perennial question remains whether or to what extent public international law has any role to play in the situation where the proper law of the contract is some municipal law, and the contract has its being in that law as the proper law of the contract. In the pages that follow it is proposed to examine the issue from the angle of the fundamental theoretical debate on the relationship between international law and municipal law, and also in the light of international case law. The topic of our discussion is not only of theoretical interest in international law but has great practical importance in the real world.

It will be observed that the monists of international law give little weight to the proper law or applicable law notion based on the doctrine of the autonomy of the will of the parties especially if the parties' choice is the law of the host state in the context of

[3] See Maniruzzaman, 'The Lex Mercatoria and International Contracts: A Challenge for International Commercial Arbitration?', 14 *American University International Law Review* (1999) 657, at 717–728; Sornarajah, 'Power and Justice in Foreign Investment Arbitration', 14 *Journal of International Arbitration* (1997) 103; Pogany, 'Economic Development Agreements', 7 *ICSID Rev-FILJ* (1992) 1, at 14 (where the author of the article, writing in 1992, affirmed the trend towards the 'localization' of state contracts in the petroleum sector, as confirmed in a number of interviews he conducted with oil industry executives). See also El-Kosheri and Riad, 'The Law Governing a New Generation of Petroleum Agreements: Changes in the Arbitral Process', 1 *ICSID Rev-FILJ* (1986) 257–258.

[4] T. Daintith (ed.), *The Legal Character of Petroleum Licences: A Comparative Study* (1981) 15.

[5] Bowett, 'State Contracts with Aliens: Contemporary Developments on Compensation for Termination or Breach', 59 *BYIL* (1988) 49, at 53. See Article 5 of the Foreign Economic Contracts Law of the People's Republic of China of 21 March 1985 in *China's Foreign Trade* (1985) No. 12; see also Article 15 of the Regulations for the Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment, 20 September 1983 in *China's Foreign Trade* (1985) No. 12. Andrews-Speed and Zhiguo Gao, 'China's Petroleum Legal Regime for Foreign Participation in Upstream Operations: The Foreign Oil Company's View', 14 *Journal of Energy and Natural Resources Law* (1996) 161, at 167. See also Mining Ordinance of Fiji, 16 December 1946, Article 56(2) (ICSID, *Investment Laws*, vol. 2); Mining and Minerals Act, Zambia 1969, Article 130 (ICSID, *Investment Laws*, vol. 10); Guatemala Regulations for the Exploration and Exploitation of Hydrocarbons of 11 January 1978, Article 168; Iranian Petroleum Act of 1974, Article 23 (see OPEC, *Selected Documents of the International Petroleum Industry, 1974* (1976) 28); Joint Structure Agreement concluded between the National Iranian Oil Co. and Amerada Hess Corp., 27 July 1971, Article 38, reprinted in 41 *Middle East: Basic Oil Laws and Concession Contracts* (Original Texts) Barrows, 23 (1974); the Service Contracts Between the National Iranian Oil Co. and Ultramar Co. Ltd, 7 August 1974, reprinted in OPEC, *ibid*, at 57, 76.

an international EDA. This is principally because of the supremacy of international law they maintain over municipal law. Furthermore, such state contracts as EDAs, although designated by the parties to be governed by the law of the host state, are no less than an internationalized contract because of the 'brooding omnipresence'[6] of international law for various subjective and objective considerations. This has created a tension in private international law that relates to the choice-of-law issue in the context of international contracts like EDAs.[7] The jurists who support the automatic internationalization of EDAs from the monist angle also justify their stance to superimpose the reins of international law on such state contracts by such subjective and objective considerations. Thus the internationalization theory turns out to be a 'cocktail theory' that serves both international law theorists (monists) and practitioners (internationalists) equally. It is noteworthy that four decades ago Professor Jennings (as he then was) observed that 'the particular topic of state contracts impinges upon some of the hardest questions of international law'.[8] The position still remains the same after so many years as far as it relates to the subject matter of our debate. It has to be recognized, however, that fewer subjects of international law have attracted so much continuous scholarly attention over the last few decades than the law governing EDAs.[9] As mentioned earlier, the purpose here is to appraise critically the fundamental question of international law, i.e. the relationship between international law and municipal law in the context of an EDA which has its only being in a municipal law, which is usually the law of the contracting host state, alone. One may start with the oft-quoted separate opinion of Judge Lauterpacht in the *Norwegian Loans* case[10] where he observed that:

> It may be admitted . . . that an 'international' contract must be subject to some national law: this was the view of the Permanent Court of International Justice in the case of the Serbian and Brazilian Loans. However, this does not mean that that national law is a matter which is wholly outside the orbit of international law. National legislation . . . may be contrary, in its intention or efforts, to the international obligations of the State. The question of conformity of national legislation with international law is a matter of international law. The notion that if a matter is governed by national law it is for that reason at the same time outside the sphere of international law is both novel and, if accepted, subversive of international law. It is not

[6] Lillich, 'The Law Governing Disputes Under Economic Development Agreements: Reexamining the Concept of "Internationalization"', in Richard Lillich and Charles Brower (eds), *International Arbitration in the Twenty-First Century: Towards 'Judicialization' and Uniformity* (1993) 92.

[7] See Weil, 'Problèmes relatif aux contrats passés entre un Etat et un particulier', 128 *Recueil des cours* (1969-III) 95, at 158. See generally Mayer, 'La neutralisation du pouvoir normatif de l'Etat en matière de contrats d'Etat', 113 *Journal du Droit International* (1986) 5.

[8] Jennings, 'State Contracts in International Law', 37 *BYIL* (1961) 156. See generally Giorgio Sacerdoti, *I Contratti tra Stati e Stranieri nel Diritto Internazionale* (1972); Philippe Leboulanger, *Les Contrats entre états et entreprises étrangères* (1985); Berlin, 'Les contrats d'Etat (state contracts) et la protection des investissements internationaux', 13 *Droit et pratique du commerce international* (1987) 197–271; Jean-Flavien Lalive, 'Contrats entre Etats ou entreprises étatiques et personnes privées. Développements récents', 181 *Recueil des cours* (1983-III) 9–283; and Pierre Lalive, *Réflections sur l'Etat et ses contrats internationaux: lecon inaugurale de l'année académique 1975–1976, donné le 20 Octobre 1975* (1976).

[9] Lillich, *supra* note 6, at 61.

[10] *Case of Certain Norwegian Loans*, ICJ Reports (1957) 9.

> enough for a State to bring a matter under the protective umbrella of its legislation, possibly of a predatory character, in order to shelter it effectively from any control by international law.[11]

The above quote has proved to be the classic statement of the monist school of thought. It has to be borne in mind that Judge Lauterpacht made this observation essentially in the context of a purely public international law judicial institution, i.e. the International Court of Justice and especially on its jurisdictional issue. However, with respect, it is noted that the adherents of this view have the tendency to generalize it irrespective of the nature of the international tribunal dealing with the matter concerned.[12] For a clear understanding it is better to investigate the spirit of this approach. Judge Lauterpacht was a naturalist, as opposed to a positivist, in the Grotian tradition.[13] Like Grotius, he believed that much of international law follows the precepts of natural law. In the Grotian legal epistemology, natural law lays the foundation for international law, and the whole edifice of international law for that matter is based on the notion of the 'social nature of man'.[14] This inspired Professor H. Lauterpacht (as he then was) to consider the individual as 'the ultimate unit of all law'.[15] Thus, in his words:

> The individual is the ultimate unit of all law, international and municipal, in the double sense that the obligations of international law are ultimately addressed to him and that the development, the well-being, and the dignity of the individual human being are a matter of direct concern of international law.[16]

Thus in Judge Lauterpacht's legal philosophy the individual is the centre of all law, international and municipal, in the context of whose unitary character international law stands as a superior legal order subordinating to it municipal law.[17] As Brownlie notes: 'in his [Lauterpacht's] work monism takes the form of an assertion of the supremacy of international law even within the municipal sphere, coupled with well-developed views on the individual as a subject of international law.'[18] He also observes that 'such a doctrine is antipathetic to the legal corollaries of the existence of sovereign States, and reduces municipal law to the status of pensioner of international law'.[19] The jurists who argue in the tune of the monist-naturalists that a state contract will always be subject to international law despite any municipal law being chosen by the contracting parties as the sole proper law of the contract may be excused for their

[11] *Ibid*, at 37.

[12] See, for example, Schwebel, 'The Law Applicable in International Arbitration: Application of Public International Law', in Albert Jan Van Den Berg (general ed.), *Planning Efficient Arbitration Proceedings: The Law Applicable in International Arbitration* (1994) 562, at 567–569.

[13] See generally H. Lauterpacht, 'The Grotian Tradition in International Law', 23 *BYIL* (1946) 23.

[14] *Ibid*, at 24–26.

[15] *Ibid*, at 27.

[16] *Ibid*, at 27.

[17] See E. Lauterpacht (ed.), *International Law, Being the Collected Papers of Hersch Lauterpacht*, vol. 1 (1970), chapter 2, 216–230.

[18] I. Brownlie, *Principles of Public International Law* (5th ed., 1998) 32.

[19] *Ibid*, at 32.

theoretical adherence.[20] Judge Lauterpacht's above-quoted observation in the context of the *Norwegian Loans* case has to be relied on very cautiously for the theory of internationalization of state contracts as it challenges the respective structural domains of municipal and international laws as perceived from the positivistic angle. Judge Fitzmaurice's caveat in this connection is quite apposite and merits citation *in extenso* as follows:

> However, in view of his finding on the jurisdictional aspects of the *Norwegian Loans* case, Lauterpacht was not called upon to go into the substantive question of whether the alleged breach of contract would in fact have involved a violation of international law. Therefore it would be wrong to attribute to him the view that if there is in fact a breach by a State of a contract between itself and a foreign national or corporate entity, a breach of international law is thereby *ipso facto* constituted, even in the absence of any denial of justice such as would result if, for instance, a right of action were not afforded to the foreigner in the local courts, or if, such a right being afforded, the decision were given against him on manifestly dishonest grounds. . .
>
> It may well be that had the Court found itself competent in the *Norwegian Loans* case, and had it gone on to determine the merits, Lauterpacht would have considered that a failure by a government to honour a gold clause in a contract with a foreigner involved a sufficiently tortious element. . . *But this cannot be assumed, and the matters seems sufficiently important and controversial to warrant this caveat against reading too much into his remarks on what was, as it then stood before him, a purely jurisdictional issue*.[21]

It is noteworthy that even Schwebel, an ardent follower of Judge Lauterpacht's view, had to concede, though reluctantly, the weight of Judge Fitzmaurice's caveat. In the words of Schwebel:

> While still other States and scholars have not accepted the position which [Judge Fitzmaurice] sets forth, and while State practice is unquestionably uneven, *it is believed that the weight of such international judgments as have been brought to bear on the question supports his view*.[22]

Thus Judge Lauterpacht's opinion in the *Norwegian Loans* case cannot be the authority for internationalization of a state contract since such a contract on its own does not create an international obligation even though international law is designated by the contracting parties to be the governing law of the contract. This is especially true in the context of any international commercial arbitration which is particularly of private international character or rather 'quasi-international'.[23] This view along the lines of general positive public international law has attracted

[20] See Schwebel, *International Arbitration: Three Salient Problems* (1987) 108–115 and 125–143; and Schwebel, *Justice in International Law* (1994) 425–435. See generally Philip Allott, *Eunomia — New Order for a New World* (1990); and Allott, 'The Concept of International Law', 10 *EJIL* (1999) 31–50.

[21] Sir Gerald Fitzmaurice, 'Hersch Lauterpacht — The Scholar as Judge: Part I', 37 *BYIL* (1961) 1, at 64–65 (emphasis added).

[22] Stephen M. Schwebel, *Justice in International Law* (1994) 427 (emphasis added).

[23] See generally F. Lalive, 'Contracts Between a State or a State Agency and a Foreign Company, Theory and Practice: Choice of Law in a New Arbitration Case', 13 *ICLQ* (1964) 987, at 997; Bourquin, 'Arbitration and Economic Development Agreements', in *Selected Readings on Protection by Law of Private Foreign Investments* (1964) 99, at 111 and 113; van Houtte, 'International Arbitration and National Adjudication', in C.C.A. Voskuil and J.A. Wade (eds), *Hague–Zagreb Essays 4 on the Law of International Trade* (1983) 312, at 322–327.

overwhelming support of jurists from both developed and developing countries.[24] Judge Fitzmaurice's aforementioned caveat reflects the international practice and the relationship between municipal law and international law in reality. One may also wonder whether Judge Lauterpacht's own attitude to the issue of the relationship between municipal law and international law is in fact always unquestionably reflected even if his *Norwegian Loans* case *dictum* is taken seriously as the monistic axiom. As Judge Lauterpacht said elsewhere:

> It will be suggested that the doctrinal controversy [regarding monism and dualism] . . . which has grown round the problem of the relation between international and municipal law, is to a large extent unreal and that, in fact, no practical consequences of importance follow from any of the solutions adopted — though in the course of the controversy doctrines have been propounded, in support of one or the other solution, which either did not, or no longer, correspond to *existing law* and which are essentially retrogressive.[25]

While stressing 'existing law' Judge Lauterpacht ventured, however, to portray the adoption or incorporation theory of international law in the monistic tune.[26] As Jenks notes: 'The relationship of international law with municipal law was one of the recurrent themes which runs through most of Lauterpacht's writing.'[27] Judge Lauterpacht strenuously tried throughout to establish the supremacy of international law over municipal law.[28] It is, however, not the purpose here to examine in detail his position on the issue. It may be noted, however, that he even went out of the way, unlike many monists, to suggest a structural innovation in the context of the relationship between international law and municipal law.[29] His suggestion as such beclouded the actual practice of states, i.e. existing law, on the issue. What his suggestion turns out to be is no less than *de lege ferenda*. For better or worse, the structure of general international law has not changed or evolved to that extent to automatically accommodate Judge Lauterpacht's wishful thinking about the relationship between international law and municipal law, at least from the strict monist standpoint.

Professor Jennings approached the matter from a different angle though, perhaps with the same result in mind. He used the private-international-law ladder to mount its subjective steps in order to reach the internationalized status of state contracts, i.e. the objective. His emphasis is first on the nexus between the contract itself (as the

[24] See Oscar Schachter, *International Law in Theory and Practice* (1991) 305–314; Brownlie, *supra* note 18, at 549–553; Sir Robert Jennings and Sir Arthur Watts, *Oppenheim's International Law*, vol. 1 (9th ed., 1992), Parts 2 to 4, 927–931; Bowett, 'Claims Between States and Private Entities: The Twilight Zone of International Law', 35 *Catholic University Law Review* (1986) 929, at 937; Stephen J. Toope, *Mixed International Arbitration* (1990) 75–90; Mann, 'State Contracts and State Responsibility', in *Studies in International Law* (1973) 302, at 309–315; C.F. Amerasinghe, *State Responsibility for Injuries to Aliens* (1967) 66–120; M. Sornarajah, *The International Law on Foreign Investment* (1994) 325–352; and M. Sornarajah, *The Pursuit of Nationalized Property* (1986) 103–108.

[25] Lauterpacht, *supra* note 17, at 153 (emphasis added).

[26] *Ibid*, at 151 *et seq*.

[27] Jenks, 'Hersch Lauterpacht — The Scholar as Prophet', 36 *BYIL* (1960) 1, at 95.

[28] Lauterpacht, *supra* note 17, at 151–177 and 216–230; H. Lauterpacht, 'Is International Law a Part of the Law of England?', in 25 *Transactions of the Grotius Society* (1940) 51–88; H. Lauterpacht, 'Decisions of Municipal Courts as a Source of International Law', 10 *BYIL* (1929) 65–95.

[29] H. Lauterpacht, 'Decisions of Municipal Courts as a Source of International Law', 10 *BYIL* (1929) 65, at 94–95.

vehicle of municipal law) and the international legal order that can be established both subjectively and objectively. He wrote:

> The first step then . . . is to establish a legal bridge between the contract and international law. An effective link must be forged between the principles of international law and the relevant municipal law, so that these two systems interact. We may find ourselves, for example, wishing to say that, even in the cases in which the contract is governed by the local municipal law as its proper law, certain overriding principles of international law impinge upon the contractual relationship itself. We can imagine a situation in which the principles of *pacta sunt servanda* or the notion of acquired rights or something of that sort operates so as to invalidate an apparent dissolution of the contract by municipal law. *The relationship between international law and municipal law must be regarded as a monist system and no longer can be explained on the basis of a dualist theory that international law and municipal law operate on different planes and never the twain shall meet*.[30]

Professor Jennings' view is based upon the unitary concept of law comprising both the branches of law, municipal and international. In his monist approach international law assumes primacy over municipal law. Such primacy is supposed to prevail in both international and municipal spheres. In fact, in fashioning his arguments Jennings was hovering on 'the possibility of an international law of contract'.[31] In his approach he seemed to have elevated the individual on the level of international law as its subject.[32] It appears clear from Jennings' view that, whether the contract is governed by municipal or international law, any simple breach of contract would be a breach of international law and would thereby engage state responsibility *vis-à-vis* the alien.[33] Thus, in his words: 'there is at any rate nothing inherent in the structure of international law, and in the relationship between international law and municipal law, that inhibits the sanctioning of contractual obligations by international law.'[34] It begs the question about the sanctioning of contractual obligations by international law since it contains no rules relevant to a

[30] R.Y. Jennings, *Rules Governing Contracts Between States and Foreign Nationals* (1965) 127–128 (emphasis added); see also Jennings, *supra* note 8, at 177–178; Sir H. Lauterpacht, in ICJ Reports (1952) 37.

[31] Jennings, *supra* note 8, at 161.

[32] See especially H. Lauterpacht, *Oppenheim's International Law*, vol. 1 (5th ed., 1935) 38; Lauterpacht, 'Is International Law a Part of the Law of England?', supra note 28, at 62–67; H. Lauterpacht, 'Régles générales du droit de la paix', 62 *Recueil des cours* (1937-IV) 129–148; H. Lauterpacht, *International Law and Human Rights* (1950); F. El-R.A. El Sheikh, *The Legal Regime of Foreign Private Investment in the Sudan and Saudi Arabia* (1984) 278.

[33] However, one may disagree that Jennings went that far if one considers his position solely from the perspective of remedies, thus: 'A termination or alteration of the contract by a change made in the proper law, though it cannot in the nature of things amount to a breach of contract in proper law, may nevertheless amount to a breach of international law. The claim may be delictual in form but it may still be a remedy in respect of the contract.' Jennings, 'State Contracts in International Law', 37 *BYIL* (1961) 156, at 181. On the Swiss–French doctrine (i.e. in the *Losinger & Co.* case, 1935 PCIJ Series C, No. 78; and the *Norwegian Loans* case, ICJ Reports (1957) 9), see Mann, *supra* note 24, at 309–315.

[34] Jennings, *supra* note 8, at 177–178.

breach of contract as such.[35] Professor Jennings also maintained: 'And if there is any point of direct contact between international law and the state contract, the theory that the only remedy for the alien contractor is for a *distinct* tort entirely independent of the contract is no longer tenable.'[36] It is interesting to note that three decades later Judge Jennings does not seem to be committed to his earlier contention. As he said:

> It is doubtful whether a breach by a State of its contractual obligations with aliens constitutes per se a breach of an international obligation, unless there is some such additional element as denial of justice, or expropriation, or breach of treaty, in which case it is that additional element which will constitute the basis for the State's international responsibility.[37]

In order to establish a link between the contract and international law, Professor Jennings resorted to different contractual elements by virtue of which the parties' intention to internationalize the contract may be presumed.[38] Such a subjective process is said to include the nature and the terms of the contract, a provision for arbitration, a stabilization clause,[39] and a choice-of-law clause.[40] Irrespective of the proper law of the contract, these contractual elements are said to forge a point of direct contact between international law and the contract. There still remains a great controversy whether the parties' true intention to internationalize the contract can be soundly presumed by such elements,[41] or, for that matter, whether they can be used as axioms for the theory of internationalization.[42] Furthermore, if the boundaries of municipal law are to be subjected to definition by such principles of international law as *pacta sunt servanda* and acquired rights in the context of state contracts, it is difficult to envisage what the advantage is. As Professor Brownlie rightly notes: 'There is no evidence that the principles of acquired rights and *pacta sunt servanda* have the particular consequences contended for.'[43] Furthermore, whatever weight was once attributed to the principles as the protective shields for foreign investors' interests in

[35] Bowett, *supra* note 24, at 936.

[36] Jennings, *supra* note 8, at 178–179.

[37] Jennings and Watts, *supra* note 24, at 929; compare Jennings, *supra* note 8, at 166–168. Cf. Garcia-Amador, 'State Responsibility in Case of "Stabilization" Clauses', 2 *Journal of Transnational Law and Policy* (1993) 23, at 32.

[38] Jennings, *supra* note 8, at 177–178.

[39] See generally Weil, 'Les clauses de stabilization ou d'intangibilité insérées dans les accords de développement économique', in *Mélanges Offerts à Charles Rousseau: La Communauté International* (1974) 301; and David, 'Les clauses de stabilité dans les contrats pétroliers — Questions d'un praticien', 113 *Journal du Droit International* (1986) 79.

[40] Weil, 'Principes généraux du droit et contrats d'Etat', in *Le Droit des Relations Economiques Internationales: Etudes Offertes à Berthold Goldman* (1982) 387; Leben, 'Retour sur la notion de contrat d'Etat et sur le droit applicable à celui-ci', in *Mélanges Offerts à Hubert Thierry* (1998) 247–280; Wengler, 'Les principes généraux du droit en tant que loi de contrat', 71 *Revue Critique en Droit International Privé* (1982) 467.

[41] See Oscar Schachter, *International Law in Theory and Practice* (1991) 305–314; M. Sornarajah, *The International Law on Foreign Investment* (1994) 327–352.

[42] See *Texaco v. Libya* (1977) 53 ILR 389; *Revere Copper & Brass Co. v. OPIC* (1978) 56 ILR 258.

[43] Brownlie, *supra* note 18, at 552; see also M. Sornarajah, *International Commercial Arbitration* (1990) 137–143; F.V. Garcia-Amador, *The Emerging International Law of Development* (1990) 123–126; and Weil, *supra* note 7, at 199.

the host state[44] seems to have waned to some extent in the face of the well-recognized 'fundamental principle of contemporary international law',[45] i.e. the principle of permanent sovereignty of states over natural resources.[46] The suitability of the principles of acquired rights and *pacta sunt servanda*[47] in the context of state contracts in contemporary international law has also been questioned by many legal scholars.[48] Too much emphasis by internationalists on the principle of 'acquired rights' or 'vested rights'[49] may prove to be rather counter-productive in the context of historic entitlements and rectification of past wrongs based on the notion of distributive justice, an aspect linked to the principle of permanent sovereignty over natural resources.[50] The notion of acquired or vested rights is not purely legal[51] but a convenient extra-legal construct, as was well explained by a scholar:

> we are driven to the conclusion that the term 'vested right' . . . is one of convenience and not of definition. It cannot mean more than a property interest, the infringement of which would shock society's sense of justice. For the idea of a 'vested right' is less legal than political and sociological. The traditions, mores, and instincts of a community determine it.[52]

Although Jennings picked up '*pacta sunt servanda*' and 'acquired rights' as the anchorage principles for internationalization of state contracts, no matter what the proper law of the contract is, he, however, did not suggest their absolute application or use as mere incantation.[53]

From the teleological point of view, a not dissimilar approach (to that of Jennings) has been made by some recent arbitral tribunals when the municipal law of the host state was considered to be the proper law of the contract. They applied international

[44] See, e.g., *German Interests in Polish Upper Silesia* case (Merits), 1926 PCIJ Series A, No. 7; *German Settlers in Poland* case, 1923 PCIJ Series B, No. 6; *Niederstrasser v. Poland, Schiedsgericht für Oberschlesien*, vol. 2, Nos 3–4; *Goldenberg and Son v. Germany*, 2 UNRIAA 909; *Sopron-Koszeg Local Railway Co*. case (1929–1930) *Annual Digest*, Case No. 34. See O'Connell, 'Economic Concessions in the Law of State Succession', 27 *BYIL* (1950) 93, at 96, note 1.

[45] Kamal Hossain and Subrata R. Chowdhury (eds), *Permanent Sovereignty Over Natural Resources in International Law: Principle and Practice* (1984) ix.

[46] See generally *ibid.*

[47] See *Amoco International Finance Corporation v. Government of the Islamic Republic of Iran*, 15 Iran–USCTR 189, at 242–243. See also generally Maniruzzaman, 'State Contracts with Aliens: The Question of Unilateral Change by the State in Contemporary International Law', 9 *Journal of International Arbitration* (1992) 141–171; Weil, 'Droit international et contrats d'État', in *Mélanges offerts à Paul Reuter: Le droit international: unité et diversité* (1981) 549, at 569; Tschanz, 'Contrats d'Etat et mesures unilatérales de l'Etat devant l'arbitre international', 74 *Revue Critique de Droit International Privé* (1985) 47.

[48] See, e.g., Sornarajah, *supra* note 43, at 137–143.

[49] The terms 'acquired' and 'vested' rights are more often than not used interchangeably in the legal literature.

[50] Oscar Schachter, *Sharing the World's Resources* (1977) 16–23, at 23.

[51] See Story, 'Property in International Law: Need Cuba Compensate US Titleholders for Nationalising Their Property?', 6 *Journal of Political Philosophy* (1998) 306, at 314–319.

[52] Anon, 'The Variable Quality of a Vested Right', 34 *Yale Law Journal* (1925) 303–309, at 307.

[53] Jennings, *supra* note 8, at 173–177.

law as a matter of incorporation. Thus, in the *Pyramids* case (also known as the *SPP* case), the ICC tribunal accepted that Egyptian law was the proper law of the contract. But the tribunal took the view that international law could be deemed as part of Egyptian law and therefore concluded that:

> We find that reference to Egyptian law must be construed so as to include such principles of international law as may be applicable and that national laws of Egypt can be relied upon only in as much as they do not contravene said principles.[54]

The tribunal's conclusion, that principles of international law override internal legislation in the event of inconsistency attributes supremacy to international law over municipal law, is generally an expression of the monist doctrine. However, the authoritative value, in view of the position of the applicable law, of such a formulation is in doubt because it is contrary to the practice of most states.[55] Moreover, party autonomy would be disregarded when it designates a particular municipal law and such designated law would be reduced to, to use Brownlie's phraseology, 'the status of pensioner of international law'.[56] It may occur to one, however, that when municipal law of the host state is the sole proper law of the contract international arbitral tribunals are sometimes prone to an idle exercise, i.e. to use an international law standard as part of the municipal law concerned even without proper research into that law. This is nothing but lip service just for the sake of it. This is dangerous.

Similar choice of law techniques were followed by an ad hoc tribunal in the *Aminoil* case.[57] The tribunal applied primarily the law of Kuwait which had, in the tribunal's view, international law as an integral part of it.[58] However, the tribunal was not faced with a conflict between a principle of international law which it considered applicable and a rule of Kuwait law. As the tribunal said: 'the different legal elements do not always and everywhere blend as successfully as in the present case.'[59] Since no conflict arose between the two laws, the issue of the primacy of the one over the other did not need to be dealt with in practice. Had there been any conflict as such, it might be that the tribunal would have attached supremacy to international law. Such a view, as also held by the ICC tribunal in the *Pyramids* case, may perhaps be an assertion that international law leaves the matters concerned entirely within the reserved domain of municipal law and when the former becomes an integral part of the latter by way of incorporation or transformation it stands as a higher norm.[60]

[54] *SPP (Middle East) Ltd and Southern Pacific Projects v. Egypt and EGOTH* [1988] LAR 309, at 330.

[55] See generally D.P. O'Connell, *International Law*, vol. I (1970) 56–79; D.W. Greig, *International Law* (1976) 55–91; Jennings and Watts, *supra* note 24, at 54–81; Butler, 'International Law and Municipal Law: Some Reflections on British Practice', in W.E. Butler (ed.), *International Law and the International System* (1987) 67; A.A. Rubano, 'The Development of Generally Recognized Rules of International Law Mentioning National Law', in W.E. Butler (ed.), *International Law and the International System* (1987) 85 (for Soviet theory of international law). See *Chung Chi Cheung v. R.* [1939] AC 167–168, *per* Lord Atkin.

[56] Brownlie, *supra* note 18, at 32.

[57] 21 ILM 976; 66 ILR 518.

[58] *Ibid*, at para. 142.

[59] *Ibid*, at para. 10.

[60] See Jennings and Watts, *supra* note 24, at 82.

According to the dualist theory,[61] though the two systems are distinct, the application of international law by way of incorporation or transformation in the municipal law is only possible because the municipal law conditions its validity and operation within the municipal sphere, and thus the municipal law assumes primacy over international law.[62] Perhaps this would be the case in most municipal courts[63] where priority will be given to an inconsistent rule of municipal law over international law in case any conflict arises between the two.[64] As to whether an international arbitration tribunal in an arbitration between a state and a foreign private party would do otherwise in these circumstances (i.e., declaring international law as an integral part of municipal law concerned and giving priority to the former in the case of conflict between the two), some distinguished scholars have expressed negative views on well-reasoned grounds.[65] However, an international tribunal should look into the municipal law practice of the state concerned and conform to it.[66] On the contrary, there are jurists who tend to entrust any kind of international arbitral tribunal, irrespective of its standing or status in international law, with the authority to rule on the relationship between international law and municipal law. As Judge Schwebel observed: 'it appears to be assumed that international arbitral tribunals, including those sitting between states and aliens, are "monist" rather than "dualist" in the place they accord to international law.'[67] We shall shortly turn to this issue again. There are also other writers who have pushed the position further, as discussed elsewhere,[68] by anchoring the contract in a basic legal order or the *Grundlegung* which is the

[61] See Morgenstern, 'Judicial Practice and the Supremacy of International Law', 27 *BYIL* (1950) 48–66.

[62] Starke, 'The Primacy of International Law', in *Studies in International Law* (1973) 159, at 160–162; see also Brownlie, *supra* note 18, at 32; G. Gaja, 'Positivism and Dualism in Dionisio Anzilotti', 3 *EJIL* (1992) 123–138.

[63] See O'Connell, *supra* note 55, at 56–79.

[64] See Jennings and Watts, *supra* note 24, at 84. Cf. Kirby, 'The Impact of International Human Rights Norms: "A Law Undergoing Evolution"', 25 *Western Australian Law Review* (1995) 1; and Kirby, 'The Growing Rapprochment Between International Law and National Law', at www.hcourt.gov.au/speeches/kirbyj/weeram.htm.

[65] See, e.g., Sornarajah, *supra* note 43, at 157.

[66] See the *Brazilian Loans* case (*France v. Brazil*), 1929 PCIJ Series A, No. 21, at 124–125; the *Serbian Loans* case, 1929 PCIJ Series A, Nos 20/21, at 46; Judge McNair, Separate Opinion, *Fisheries* case, ICJ Reports (1951) 181; and Judge Klaestad, Dissenting Opinion, *Nottebohm* case (Second Phase), ICJ Reports (1955) 28–9. See also the *Lighthouses* case, 1934 PCIJ Series A/B, No. 62, at 22; and the *Panevezys–Saldutiskis Railway* case, 1939 PCIJ Series A/B, No. 76, 19; the *Schooner Jane*, 37 Ct Cl. 24, at 29 (1901); the *Ship Rose*, 36 Ct Cl. 290, at 301–302 (1901); the *Schooner Nancy*, 27 Ct Cl. 99, at 109 (1892); *Re Mittermaier* (1946) *Annual Digest*, Case No. 28; Tesón, 'The Relations Between International Law and Municipal Law: The Monism/Dualism Controversy', in M. Bothe and R.E. Vinuesa (eds), *International Law and Municipal Law* (German–Argentinian Constitutional Law Colloquium, 1982) 107, at 111–112; and Brownlie, *supra* note 18, at 40.

[67] Stephen M. Schwebel, *International Arbitration: Three Salient Problems* (1987) 140.

[68] See Maniruzzaman, 'Choice of Law in International Contracts — Some Fundamental Conflict of Laws Issues', 16 *Journal of International Arbitration* (1999) 141, at 152–154.

international legal order.[69] The contract derives its binding force from such a legal order, as does its proper law. The concept of internationalization of contract via the *Grundlegung* doctrine is, however, a matter of great controversy.[70]

The supremacy of international law over municipal law has been denied by many writers when municipal law is the exclusive choice of law. Thus, in the words of Dr Mann:

> as a matter of public international law no State can rely on its own legislation to limit the scope of its international obligations. But this rule contemplates obligations governed by public international law and has no bearing upon the scope of obligations which are subject to a system of municipal law, such as the law of the debtor State. If under the latter system of law no breach of contract occurs, it is not open to public international law to assert the contrary. Where the debtor State does wrong to its alien creditor, public international law may impose a delictual liability. The existence of a tort towards the creditor's State is independent of any question of breach of contract.[71]

The contractual nexus is thus regarded as a closed system within its own proper law. This view has attracted vigorous support in the recent legal literature on the subject.[72] Dr Mann defended his thesis that: 'To hold the parties to their own choice of a legal system as the proper law of their contract and to judge the existence or non-existence of a "breach" by the law so chosen is imperatively demanded by any legal order which cherishes certainty, equitable treatment, and sound results.'[73] So there can be no 'breach' of contract unless there is a breach in the proper law, and no law other than the proper law of contract can establish one.[74] Thus, when municipal law is the proper law of the contract, and the contract is changed according to that law or by virtue of that law, there cannot be any breach of contract in international law.[75] Dr Mann's view has not only underscored the exclusiveness of the proper law as far as the rights and obligations of the parties to a contract are concerned but also the distinctiveness of the two systems of law, namely, municipal and international law,

[69] See, e.g., Weil, *supra* note 47, at 558; Verhoeven, 'Arbitrage entre Etats et entreprises étrangères: des règles spécifiques?', in *Hommage à Jean Robert, Les Etats et l'arbitrage international, Rev. Arb.* (1985) 609, at 627–28; Mayer, 'Le mythe de "l'ordre juridique de base" (ou Grundlegung)', in *Le Droit des Relations Economiques Internationales: Etude Offertes à Berthold Goldman* (1982) 199.

[70] See Maniruzzaman, *supra* note 68, at 152–154.

[71] Mann, *supra* note 24, at 315; S.K.B. Asante, 'Stability of Contractual Relations in the Transnational Investment Process', 28 *ICLQ* (1979) 401, at 406. See also the *Serbian Loans* case, 1929 PCIJ Series A, No. 20, at 20; and the *Norwegian Loans* case, ICJ Reports (1957) 31.

[72] See Bowett, *supra* note 24, at 932, note 12; Delaume, 'The Proper Law of State Contracts and the Lex Mercatoria: A Reappraisal', 3 *ICSID Rev-FILJ* (1988) 79; and Asante, *supra* note 71, at 406.

[73] Mann, *supra* note 24, at 315.

[74] The preliminary question of whether or not there is a breach of contract is to be determined by the proper law of the contract. The idea of submitting questions of breach of contract between a state and a private party to the proper law was adopted in Article 12(1) of the 1961 Harvard Draft Convention on the Responsibility of States. See Baxter and Sohn, 'Convention on the International Responsibility of States for Injuries to Aliens', 55 *AJIL* (1961) 545, at 548 *et seq*.

[75] See generally A.A. Fatouros, *Government Guarantees to Foreign Investors* (1962); Bowett, *supra* note 24, at 936–937.

which operate in their own respective spheres without interacting with each other,[76] when one or the other is the proper law of the contract.[77] It seems that Dr Mann would not object to the interaction of municipal and international laws when both laws are jointly the designated proper law of the contract. Thus, for him, it is the proper law that matters, and not the interaction itself between the two if it is permitted in the choice-of-law provision. For the justification of his thesis, he resorted to the private international law of the forum of arbitration, i.e. the *lex fori* theory.[78] He suggested that 'we must still start from private international law to subject the contract to international law'.[79] This leads us back to the dualist square through the alleyway of private international law once again. The positivists may find justification for Dr Mann's view even in public international law.[80] It thus appears from Dr Mann's standpoint of the jurisdictional theory of arbitration[81] that an international arbitral tribunal is bound by the approach to international law adopted by the national courts of the arbitral forum or the seat of the arbitral tribunal, i.e. the *lex fori*. This is perhaps to affirm the supremacy of municipal law over international law from the standpoint of municipal courts. As alluded to earlier, in state practice there seems to be a tendency for municipal courts to apply municipal law when it is inconsistent with international law unless the former has made a provision for the application of the latter.[82] However, it cannot be denied that there is a strong emerging theory of delocalization of international arbitration as opposed to the *lex fori* theory.[83] This does not necessarily mean that under this delocalization theory an international arbitral tribunal can override the parties' choice of municipal law as the sole proper law of the contract and apply a-national law or rules in disregard of the parties' mandate for the tribunal as some internationalists[84] (whether they are dedicated monists or else) or

[76] See also Fitzmaurice, 'The General Principles of Law', 92 *Recueil des cours* (1957-II) 1, at 68–94 especially at 70.

[77] Mann, *supra* note 24, at 315.

[78] F.A. Mann, *Studies in International Law* (1973) 257, at 262 *et seq*; Mann, 'Lex Facit Arbitrum', in Pieter Sanders (ed.), *International Arbitration Liber Amicorum for Martin Domke* (1967) 157, at 159–162.

[79] Mann, 'The Theoretical Approach Towards the Law Governing Contracts Between States and Private Persons', 11 *Revue Belge de Droit International* (1975) 562, at 586, and *ibid*, at 594; Mann, 54 *AJIL* (1960) 572, at 580; and W.M. Reisman, *Systems of Control in International Adjudication and Arbitration: Breakdown and Repair* (1992) 134–139.

[80] Reisman, *supra* note 79, at 136.

[81] See Maniruzzaman, 'State Contracts and Arbitral Choice-of-Law Process and Techniques — A Critical Appraisal', 15 *Journal of International Arbitration* (1998) 65, at 66–68.

[82] Cf. Schwebel, *supra* note 67, at 142–143.

[83] See Sandrock, 'How Much Freedom Should an International Arbitrator Enjoy? — The Desire for Freedom from Law v. the Promotion of International Arbitration', 3 *American Review of International Arbitration* (1992) 30; von Mehren, 'To What Extent is International Commercial Arbitration Autonomous?', in *Le Droit des Relations Economique Internationales Etude Offerte à B. Goldman* (1982) 217; Paulsson, 'Delocalisation of International Commercial Arbitration: When and Why It Matters', 32 *ICLQ* (1983) 53; Paulsson, 'The Extent of Independence of International Arbitration from the Law of the Situs', in J.D.M. Lew (ed.), *Contemporary Problems in International Arbitration* (1986) 141; Maniruzzaman, *supra* note 81, at 66–72. See also Borches, 'The Internationalization of Contractual Conflicts Law', 28 *Vanderbilt Journal of Transnational Law* (1995) 421; Baxter, 'International Business Disputes', 39 *ICLQ* (1990) 288, Baxter, 'International Conflict of Laws and International Business', 34 *ICLQ* (1985) 538.

[84] See Schwebel, *supra* note 67, at 125–143.

mercatorists[85] may contend.[86] It is well recognized that the parties' choice of law in a contractual situation is upheld both by private international law and public international law. There is no doubt that the principle of party autonomy in the matter of choice of law is also a principle of public international law as it is a universally accepted principle of private international law.[87] Thus there is nothing in the structure of contemporary general international law that overrides the party autonomy in the matter of choice of law and for that matter superimposes international law on the parties' choice of a municipal law in a contract.

As a matter of fact, there occurs a common field of operation for both municipal and international laws by virtue of the autonomy of the will of the parties to a contract when both are jointly the proper law of the contract. There remains to be determined the operational relationship between the two systems. In the *Texaco* case, where the two-tier system occurred as the proper law, municipal law was reduced to the status of *renvoi*.[88] This is perhaps due to the fact that the tribunal held the contract to be rooted in the international legal order, i.e. *Grundlegung* or the basic legal order.

In view of such a state of internationalization of the contract, had there been only municipal law as the single proper law of the contract, it would have been similarly given the *renvoi* status.[89] This would certainly be an extreme case and a manifestation of the monist doctrine. It would disregard the party autonomy for the proper law of the contract. However, in the case of such a two-tier system of proper law (i.e., municipal and international laws) one may resort to the wisdom of the second sentence of Article 42(1) of the ICSID Convention[90] on the operational relationship between the two.[91] Perhaps with the same result in mind, Professor Lipstein suggested that:

> The better view seems to be that such a combination of municipal law and international law

[85] See W.M. Reisman, *Systems of Control in International Adjudication and Arbitration: Breakdown and Repair* (1992) 138.

[86] See Maniruzzaman, *supra* note 3, at 678–680.

[87] Jennings, *supra* note 8, at 178.

[88] *Texaco v. Libya*, 53 ILR 389, at 460 (para. 50); see also Weil, 'Les clauses de stabilisation ou d'intangibilité insérées dans les accords de développement économique', in *Mélanges Offerts à Charles Rousseau: La Communauté International* (1974) 301, at 319–320. Cf. Lipstein, 'International Arbitration Between Individuals and Governments and the Conflict of Laws', in *Essays in Honour of Schwarzenberger* (1988) 177, at 182.

[89] See ICC Case 4761 (1984), reported in *Clunet* (1986) 1137. Although this case was concerned with Italian and Libyan private parties, the tribunal held that the contract was subject to 'international public order' even though it had been determined that Libyan law should govern.

[90] Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, 1 ICSID Reports (1965) 3 *et seq*.

[91] See Broches, 'The Convention on the Settlement of Investment Disputes Between States and Nationals of Other States', 136 *Recueil des cours* (1972-II) 331, at 392 *et seq*; Shihata and Parra, 'Applicable Substantive Law in Disputes Between States and Private Foreign Parties: The Case of Arbitration Under the ICSID Convention', 9 *ICSID Rev-FILJ* (1994) 183; M. Hirsch, *The Arbitration Mechanism of the International Centre for the Settlement of Investment Disputes* (1993); Maniruzzaman, 'International Commercial Arbitration: The Conflict of Laws Issues in Determining the Applicable Substantive Law in the Context of Investment Agreements', 40 *Netherlands International Law Review* (1993) 210, at 233–235.

> only introduces standards which delimit the application of the municipal laws selected by the parties, but which cannot prevail over specific references to a particular legal system.[92]

However, it cannot be denied that one of the parties to a state contract, i.e. the state, is a subject of international law, and that that law governs its conduct by providing certain international minimum standards with respect to the treatment of aliens. And no matter what the choice of law of the contract is, whether municipal or otherwise, since one of the parties to such a contract is a sovereign state the international minimum standards of state conduct must apply to that effect.[93] If the host state's law is the only designated proper law of the contract, it must conform to the requirements laid down by international law governing the conduct of states. From this perspective, international law is to that extent supreme over municipal law as an objective standard.[94] Most legal systems do in fact conform to such international law requirements of a lawful exercise of a state's prerogative rights *vis-à-vis* aliens.[95] Professor Bowett has observed that:

> the argument that the State's conduct is governed by international law adds very little to the substantive requirements *except* in the extreme situation of a State claiming, by virtue of its own municipal law, prerogatives not generally recognized to the State under most systems of law, such as the right to discriminate against aliens or the right to refuse all compensation.[96]

By saying that the specific municipal law as the sole proper law of the contract must conform to the requirements laid down by international law governing the conduct of states is not to suggest that international law supplants the proper law as the system in which the contract has its being.[97] Here we have signified the relevance of international law to the extent of international minimum standard, and not the lock, stock and barrel of international law, i.e. international law as the whole system. However, the controversy with regard to the content and scope of international minimum standards in contemporary international law is another matter.[98] It is though expected that an international arbitral tribunal will have a sympathetic ear to

[92] Lipstein, *supra* note 88, at 182; see also Delaume, 'State Contracts and Transnational Arbitration', 75 *AJIL* (1981) 784, at 798.

[93] Jennings, *supra* note 8, at 181–182; see also Bowett, *supra* note 24, at 936–937; and Olmstead, 'Economic Development Agreements Between States and Aliens: Choice of Law and Remedy', 48 *California Law Review* (1960) 424.

[94] Jennings, *supra* note 8, at 179.

[95] See Jennings and Watts, *supra* note 24, at 81–82; Delaume, *supra* note ***, at 90.

[96] Bowett, *supra* note 24, at 937.

[97] Jennings, *supra* note 8, at 181.

[98] See Adede, 'The Minimum Standards in a World of Disparities', in R.St.J. Macdonald and D.M. Johnston (eds), *The Structure and Process of International Law* (1983) 1001, at 1004–1005; Borchard, 'The "Minimum Standard" of the Treatment of Aliens', 38 *Michigan Law Review* (1940) 445; Allan Roth, *The Minimum Standard of International Law Applied to Aliens* (1949) 72–74; Maniruzzaman, 'Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview', 8 *Journal of Transnational Law and Policy* (998) 57.

the pleading of international law by a foreign investor,[99] but it cannot be guaranteed except in the limited sense when the municipal law of the host country is the sole and exclusive choice of law. It thus sounds plausible to pay heed to Professor Higgins' sage counsel as she says:

> Of course, the best way to avoid sole reliance on domestic law is, one has to say, by having a governing law clause that introduces international law. If, in the bargaining process, the private party has been unable to accomplish this, it seems doubtful that international arbitrators should remedy that which one of the negotiating parties was unable to achieve.[100]

Looked at from the standpoint of private international law, the freedom of choice (autonomy of will) of the parties should, in principle, be respected, which is also a rule of international law. Thus, Professor Bowett is right when he said, while commenting on the *Pyramids* case, that:

> whenever there is a contractual choice of a specific municipal legal system as the proper law, the choice is to that legal system per se. There is no *renvoi* to international law, and thereby to other municipal systems generally, via the concept of 'general principles of law' as a part of international law.[101]

In a similar vein, Professor Brownlie seems to have supported this position in principle when he states that 'an express choice of municipal law should not be subverted by the insertion of public international law'.[102]

The above observations also apply in the context of the first sentence of Article 42(1) of the ICSID Convention. When the choice of law is solely the host state's or any other domestic law, the question arises whether international law applies, and, if it applies, then to what extent it applies. Obviously, there is no doubt that international law may apply to the extent that it is incorporated in the domestic law concerned. As mentioned earlier, because the state is a party to a contract, its conduct will be governed by international minimum standards as mandatory rules of international law which is independent of any conflict rules.[103] This means that, according to the first sentence of Article 42(1), whatever law the parties choose other than international law such mandatory rules of international law will inevitably apply.[104] In other words, such mandatory rules will be superimposed on the parties' choice. This is not to imply that, despite the parties' exclusive choice of a domestic law or municipal law, international law will apply in its expansive sense as it is provided in

[99] Jaenicke, 'The Prospects for International Arbitration: Disputes Between States and Private Enterprise', in A.H.A. Soons (ed.), *International Arbitration: Past and Prospects* (1990) 155, at 158; Jaenicke, 'Consequences of a Breach of an Investment Agreement Governed by International Law, by General Principles of Law or by Domestic Law of the Host State', in D.C. Dicke (ed.), *Foreign Investment in the Present and a New International Economic Order* (1987) 177, at 181–182.

[100] Rosalyn Higgins, *Problems and Process: International Law and How We Use It* (1994) 141.

[101] Bowett, *supra* note 24, at 932, n. 12.

[102] Brownlie, 'Some Questions Concerning the Applicable Law in International Tribunals', in J. Makarczyk (ed.), *Theory of International Law at the Threshold of the 21st Century: Essays in Honour of Krzysztof Skubiszewski* (1996) 763, at 767.

[103] Schreuer, 'Commentary on the ICSID Convention: Article 42', 12 *ICSID Rev-FILJ* (1997) 398, at 443.

[104] *Ibid*, at 443.

the second sentence of Article 42(1).[105] This is true in the case of the ICSID tribunal as it is in the case of any other international commercial arbitral tribunal. A few comments are in order in this context and we shall shortly turn to the ICSID matter again. It is not questioned whether an alien has the right to plead international law before an international commercial arbitral tribunal.[106] Certainly, international law may be pleaded if it is the parties' choice in a state contract. However, again, the nature and extent of the application of international law to a state–alien contractual situation by an international commercial arbitral tribunal has given rise to controversies amongst jurists. The answer to this issue seems to depend upon the nature of the international arbitral tribunal itself in international law and the authority given to it by its governing constitutive instruments. These aspects may also have a bearing upon the question whether an international arbitral tribunal can supplement the parties' choice of law or even override it by a-national rules or principles, whether international or otherwise. Thus, for instance, in the practice of the Iran–United States Claims Tribunal, it is found that the Tribunal on some occasions disregarded the parties' choice of law and applied a-national rules or principles as the Claims Settlement Declaration (CSD) authorized it to do.[107] Article V of the CSD provided the Tribunal with a broad discretion in its choices of applicable law[108] by virtue of which it was possible to disregard the parties' choice.[109] Another example could be the ICC Tribunal which by virtue of Article 17(2) of the 1998 ICC Rules of Arbitration is authorized in all cases, whether in the case of an express choice of law or in the absence of it, to take account of the relevant trade usages. This may mean that, if the parties' chosen law is inconsistent with the relevant trade usages, the latter may override the chosen law to the extent of its inconsistency. In a similar vein, one may also point to the authority of the tribunals established under the North Atlantic Free Trade Agreement (NAFTA)[110] and the Energy Charter Treaty (ECT),[111] which are recent phenomena, to decide the issues in dispute in accordance with relevant treaty provisions and applicable rules and principles of international law, no matter what the parties may expressly choose to the contrary in their investment contracts. This means that, even if the parties to a contract choose national law as the

[105] See the 'Report of the World Bank Executive Directors on the ICSID Convention', in Doc. ICSID/2, para. 40.

[106] Cf. Schwebel, *supra* note 67, at 125–143.

[107] See, e.g., *CMI International Inc. v. Ministry of Roads and Transportation et al.*, 4 Iran–USCTR 263.

[108] Article V of the Claims Settlement Declaration provided that: 'The Tribunal shall decide all cases on the basis of respect for law, applying such choice of law rules and principles of commercial and international law as the Tribunal determines to be applicable, taking into account relevant usages of the trade, contract provisions and changed circumstances.' See George H. Aldrich, *The Jurisprudence of the Iran–United States Claims Tribunal: An Analysis of the Decisions of the Tribunal* (1996) 156–170.

[109] See, e.g., *CMI International Inc. v. Ministry of Roads and Transportation et al.*, 4 Iran–USCTR 263, at 267–268.

[110] Article 1131(1).

[111] 34 ILM (1995) 360, Article 26(6).

governing law or in the absence of such a choice the conflict of laws rules lead to the application of national law, a NAFTA or ECT arbitral tribunal will accord supremacy to relevant treaty provisions and applicable international law rules. In any event, the application of national law or anything else which the parties may have agreed to be applicable is controlled by the aforesaid standards provided in the treaties.[112] These special features stem from the very nature of the tribunals owing to their constitutive instruments to which the parties voluntarily subject their choice of law. These regimes may be better considered to be the *lex specialis*. It is here, it is believed and rightly so, that Judge Schwebel's claim (as mentioned earlier) that international arbitral tribunals are 'monist' rather than 'dualist' in the place they accord to international law, is justified. Thus this claim bears on the true international character of the tribunal because of its constitutive instruments which authorize it to behave in that specific way in positive international law. The authority to question, in the monist tone, a state's international responsibility for its breach of an international obligation in the context of state–alien contractual relations, lies with such a tribunal. The claim by any other international commercial arbitration of private character to act as 'monist' would be a claim that far exceeds its status as a tribunal and belies positive international law. Had that not been the case, there would not have been any need to devise the regime of such *lex specialis* as highlighted above. From both international diplomatic and positive international law standpoints, it is neither desirable nor practical to allow a 'quasi-international' arbitral tribunal to behave like a truly international arbitral tribunal and to call into question a state's international responsibility for its actions towards an alien contractual partner. However, apart from the aforementioned regime of *lex specialis*, there still remains a burning controversy as to the relevance of international law and also the extent of its relevance to a state contract when a domestic law is its sole chosen proper law.[113]

Now turning to the ICSID scene once again, there seems to be a tendency in the views of some writers to blur the boundary between the first and the second sentences

[112] See Wälde, 'Investment Arbitration Under the Energy Charter Treaty — From Dispute Settlement to Treaty Implementation', 12 *Arbitration International* (1996) 429, at 457–458; Tucker, 'The Energy Charter Treaty and "Compulsory" International State/Investor Arbitration', 11 *Leiden Journal of International Law* (1998) 513, at 524–525; Price, 'An Overview of the NAFTA Investment Chapter: Substantive Rules and Investor–State Dispute Settlement', 27 *International Lawyer* (1993) 727; Delaume, 'Consent to ICSID Arbitration', in Joseph J. Norton *et al.* (eds), *The Changing World of International Law in the Twenty-First Century: A Tribute to the Late Kenneth R. Simmonds* (1998) 155, at 172–174.

[113] Cf. generally the International Law Commission Reports on 'International Responsibility' by Dr F.V. Garcia Amador as its Special Rapporteur: *Yearbook of the International Law Commission*, vol. II (1956) 173; *Yearbook of the International Law Commission*, vol. II (1958) 47; and *Yearbook of the International Law Commission*, vol. II (1960) 41.

of Article 42(1) of the ICSID Convention as far as it relates to international law.[114] This has been reflected in both the *LETCO*[115] and *SPP*[116] decisions where the ICSID tribunals applied international law in the expansive sense as understood in the context of the second sentence of Article 42(1) despite the parties' choice of the respective host states' law. In these two cases the tribunals' approaches suggest that no matter what law is chosen by the parties, according to the first sentence of Article 42(1), international law applies either as a controlling system or has a gap-filling function as under the second sentence. In the *SPP* case, the tribunal resorted to international law, according to the second sentence, to fill the gap in Egyptian law, which the tribunal did not deny as the law chosen by the parties. The tribunal held:

> [E]ven accepting the Respondent's view that the Parties have implicitly agreed to apply Egyptian law, such an agreement cannot entirely exclude the direct applicability of international law in certain situations. The law of [the Arab Republic of Egypt], like all municipal legal systems, is not complete or exhaustive, and where a lacunae occurs it cannot be said that there is agreement as to the application of a rule of law which, *ex hypothesi*, does not exist. In such case, it must be said that there is 'absence of agreement' and consequently, the second sentence of Article 42(1) would come into play.[117]

If it is in fact or accepted that a choice of a domestic law or any other law has been made by the parties and there proves to be lacunae in such law, the tribunal's approach to international law, as under the second sentence of Article 42(1) above, is far-reaching,[118] dangerous and quite contrary to the spirit of the ICSID Convention. This approach will practically render the first sentence of Article 42(1) meaningless.[119] According to the first sentence, the tribunal must in principle respect the parties' intention and freedom of choice of law. This is the mandate of the Convention for the tribunal concerned. The tribunal should not rewrite the parties' choice and such autonomy of the will of the parties has also been preserved in the Convention. In principle, the tribunal should fill the lacunae in the chosen law of the parties according to the gap-filling mechanism offered by that chosen law[120] and that will conform to the mandate of the tribunal in the first sentence of the Article. If any tribunal violates this, it will be in breach of its mandate given by the Convention. In fact, such gap-filling mechanisms are usually found in municipal laws.[121] If the lacunae in the chosen law

[114] E. Lauterpacht, 'The World Bank Convention on the Settlement of International Investment Disputes', in *Recueil d'Etudes de Droit International et Hommage à Paul Guggenheim* (1968) 642, at 660; Goldman, 'Le droit applicable selon la Convention de la BIRD du 18 Mars 1965, Pour le réglement de Differends Relatifs au Investissements entre Etat et ressortissants d'autres Etats', in *Investissements Etrangers et Arbitrage entre Etats et Personnes Privés: La Convention BIRD du 18 Mars 1965* (1969) 133, at 151.

[115] *LETCO v. Liberia*, Award, 31 March, 2 ICSID Reports 358.

[116] *Southern Pacific Properties (Middle East) Ltd v. Arab Republic of Egypt*, Case No. ARB/84/3, 8 *ICSID Rev-FILJ* (1993) 328 (hereinafter the *SPP* Award).

[117] *Ibid.*, at para. 80.

[118] Schreuer, *supra* note 103, at 440.

[119] Delaume, 'The Pyramids Stand — The Pharaohs Can Rest in Peace', 8 *ICSID Rev-FILJ* (1993) 231, at 248.

[120] *Ibid.* See *supra* note 66. Chukwumerije, 'International Law and Article 42 of the ICSID Convention', 14 *Journal of International Arbitration* (1997) 79, at 86.

[121] See the *SPP* Award, the Dissenting Award, in 8 *ICSID Rev-FILJ* (1993) 400, at 482–483.

is equivalent to the absence of choice as understood in the second sentence of Article 42(1) it would have to be clearly provided as such, and to hold otherwise would be contrary to the construction of the Article.[122]

[122] See Nassar, 'Internationalization of State Contracts: ICSID, the Last Citadel', 14 *Journal of International Arbitration* (1997) 185.