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REPORT ON CERTAIN ISSUES RELATING TO THE JOINT STUDY ON INTERNATIONAL INDUSTRIAL CO-OPERATION 1/

by

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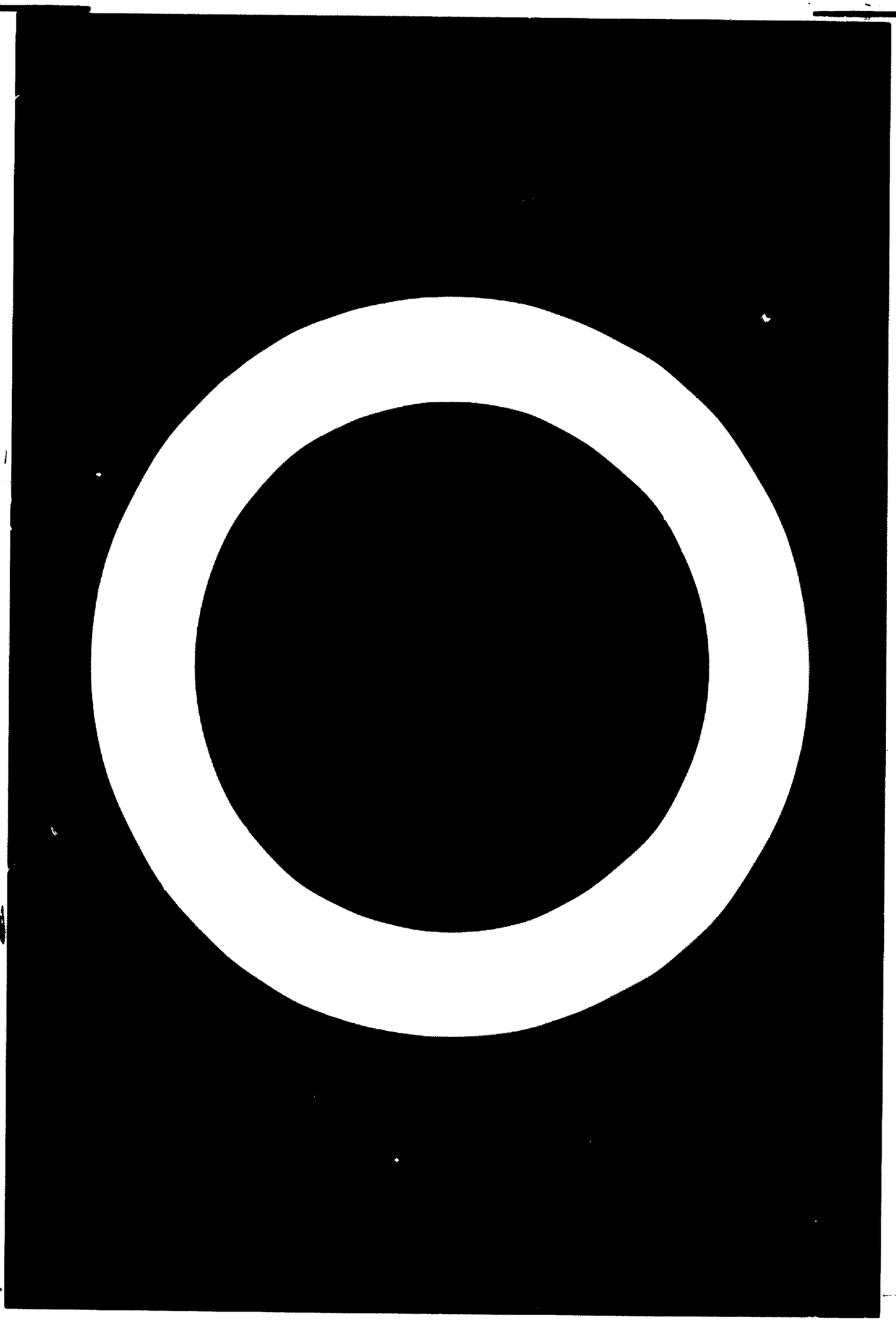

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1) I. BACKGROUND

On 28 January 1977, I was invited by the International Center for Industrial Studies (UNIDO Secretariat) to advise them on certain legal and commercial issues relating to the Joint Study on international industrial cooperation, and was requested to prepare a report on the issues discussed on that occasion.

2) This report, submitted on 23rd February and slightly revised thereafter, sets out these issues in their general legal framework so that specific problems may be seized in their context and evaluated in their comparative importance. Thus, the report, while pointing out some of the specific problems of industrial cooperation and the directions for possible solutions, also provides for a conceptual framework of the legal aspects of the Joint Study.

3) It should be pointed out that many of the issues referred to in this report are very complex and controversial. The report, therefore, simply points out some of the salient aspects of these issues and does not purport to go into an exhaustive description of the full range of problems and controversies on the subject nor does it attempt to spell out all of the suggested and adopted solutions.

II. FORMS OF INTERNATIONAL INDUSTRIAL COOPERATION

4) When the developing countries, in the process of their industrialization, refer to international cooperation, two forms of this cooperation may be distinguished.

A. Industrialization contracts*:

5) The Government, a public corporation or a private party in the developing country ("the developing party"*) may enter into contractual arrangements with a public or private party in an industrialized country ("industrial party"*), for the purchase of equipment, technology or services (e.g. contract for the purchase of a factory on a turn-key basis, licensing contracts or arrangements for the management of a firm or for the marketing of its products).

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* The terms "industrialization contract", "developing party" and "industrial party" are tentative; further exploration of the subject may lead to a preference for a different terminology. "Industrialization contract" was chosen to emphasize the function which a particular contract for purchase of equipment or the management of a new factory plays in the context of the national development policy. The term "industrial party" should point out the party supplying the goods or services for the industrialization; it does not mean that this party necessarily is a firm in an industrialized country; such goods and services may on occasion also be supplied by a party in another developing country and it would appear as one of the most important objectives of an international industrialization policy to increase the number of cases where these goods and services are supplied by other developing countries.

6) The resources by which the developing party pays the industrial party may be raised locally or through international loans; in both cases, the developing party has to provide the funds irrespective of the success or failure of the operation. In other words, the developing party has full control over the operation and bears the risk of its failure, and reaps the profits of its success.

B. Foreign investment

7) The transfer of resources may occur also by way of foreign investment. Without entering into the dispute as to the exact definition of the term "foreign investment", it may be said that in its basic form foreign investment results from a unilateral decision of the industrial party to transfer assets (funds, capital goods, know-how or services) to the developing country without an immediate remuneration. The remuneration of this transfer occurs only in case of success of the venture. In this form, the foreign investment does not require contractual arrangements; nevertheless the investment often goes along with an agreement concluded between the industrial party and public authorities of the developing country, providing for certain aspects of the relationship between the public authorities and the foreign industrial party (in particular certain privileges with respect to taxation, customs, etc. and the integration of the foreign investment into the national economic context.)

8) Both forms of industrial cooperation have their advantages and disadvantages and the choice of either form depends on a number of considerations, among which the most important ones seem to be those

related to basic options of national economic policy and the general economic situation of the developing country in question : in fact foreign investment in centrally planned economies is very difficult to realize, although not impossible; on the other hand the decision of a foreign investor to set up an operation in a given country depends on a number of criteria (in particular existence of an attractive market and natural resources) on which the developing country in question has little influence; and of course industrialisation contracts require availability of funds either in the form of savings or through access to the international financing.

9) In recent times, the distinction between the above mentioned two forms of industrial cooperation at least in some cases is beginning to become less marked in view of attempts to combine the advantages of both forms of cooperation, e.g. purchase of a factory on a turn-key or even as a going concern, coupled with a contract for management and arrangement for payment on conditions related to the results achieved by the factory . Such attempts deserve particular attention. But for clarity's sake this report follows for its main part the distinction between investment and industrialization contracts, as outlined above.

III. THE FRAMEWORK IN WHICH INDUSTRIAL COOPERATION TAKES PLACE

A. Foreign investment

1) Measures taken by the host country

10) When Governments choose to pursue an economic development policy which attributes a major role to foreign investment, they frequently provide a set of measures whereby they hope to attract such foreign investment. Such "investment incentives" consist in favourable treatment of requests for foreign currency for the purchase of goods, equipment and services as well as for the transfer of profits and liquidation proceeds, work permits, financial facilities in the form of preferential loans access to the local financing market, or even grants and a number of other facilities. There seems to be no uniformity among economists with respect to the effectiveness of such investment incentive programs and it may well be that, in cases, the advantages granted to the foreign investor create a burden on the developing country which exceeds the profits it reaps from the investment. And not always is it possible to avoid some sort of competition among developing countries in their investment incentive programs.

11) In recent times, an increasing number of countries have been giving special attention to a set of laws and regulations which may somehow be considered as the counter-part to the investment incentives: these laws provide for special regulations applicable

to foreign investment in order to ensure that such investment conforms to the options of the national development policy. Such "regulating legislation" which often is conceived as a defense against the abuse of power by multinational corporations deals with such subjects as:

- control over local entreprises,
- conditions of exploitation of natural resources,
- contractual arrangements especially with other firms of the same group,(a particular point in issue are transfer prices, i.e. prices paid by the firm in the developing country to the mother company or another company of the same group abroad for goods, services or know how)
- profits of the entreprise and the shares of these profits which may be distributed and those which have to be reinvested,
- employment of aliens,
- access to the local capital market.

Some countries provide that foreign investment is restricted to certain branches of the economy or certain activities.

12) Many of the provisions concerning foreign investment, in particular those of a regulatory nature, are applicable ipso facto to any foreign investment. Others, and specially some of the investment incentives, are applicable only on a case to case basis and require either a unilateral decision by a public authority or an agreement with the investor. The investor himself often seeks to conclude with the public authority an agreement

spelling out the conditions under which he may conduct his business and the advantages granted to him. He will try in particular to obtain a stabilization clause (a clause excluding unilateral changes of the legal conditions under which the investment is carried out) and a provision for the settlement of disputes. It appears that contracts protecting the rights of the investor are rather frequent but it would appear that a much smaller number of contracts assure the Government that the expectations which it had when granting the investment incentives will actually be fulfilled.

2) Investment promotion in the country of origin

13) A number of capital exporting countries provide a system of so-called investment protection measures : such measures are primarily a system of insurance against political risks, i.e. losses suffered by the investor which are not due to economic reasons but to political decisions by the host country. The oldest and most developed systems are those of the USA dating back to 1948, of Japan (since 1956), and of the Federal Republic of Germany, (since 1959). Protection is provided only in case of approved investments in the developing countries with the notable exception of the Japanese system which applies to all foreign investment of Japanese firms. However, insurance of an investment project in a developing country in most cases, is granted only if a bilateral agreement has been concluded between the country of origin and the host country, again with the notable exception of Japan.

3) International arrangements

14) In general, the home country provides such investment insurance only if it has previously concluded an inter-Governmental agreement with the host country. This has led to a wide network of such "umbrella agreements" (generally under the title of "Treaty of Friendship, Commerce and Navigation" - TFCN - in the case of the USA and "Investitionsschutzverträge" in the case of the Federal Republic of Germany).

15) Although these agreements generally provide equal treatment for both parties (i.e. each party engages itself to afford a certain treatment to investment of nationals of the other party), the difference in the factual situation makes the apparent reciprocity rather illusory. In fact, these bilateral investment protection treaties themselves are rather unequal since the interests of the capital importing country are dealt with only marginally. These interests are protected insofar as generally the provisions of the treaties apply only to investment projects approved by the host country.

16) While the existence of such bilateral investment protection treaties is quite useful in providing an international legal framework at least for some investment projects, the disadvantages of this system should not be overlooked : it is limited to nationals of a very few capital-exporting States and thus is inapplicable to large-scale multinational investment projects. Moreover, it contains the risk of diplomatic antagonisms between the States involved

17) In order to avoid the disadvantages of bilateral investment protection, a number of attempts have

been made to create multilateral schemes for the ensurance of foreign investment.(e.g. IBRD and Council of Europe drafts)or for investment protection in general (e.g. OECD draft Convention, Abs - Shawcross Draft), none of which have succeeded until now. The only successful project on a multilateral level englobing industrialised countries and developing countries is the Convention for the Settlement of Investment Disputes between States and Nationals of Other States signed in Washington in 1965, which is limited to the settlement of investment disputes. It will be referred to below in the context of settlement of disputes. Among the attempts for a regional solution of multilateral investment insurance, special mention must be made of the Inter Arab Investment Insurance scheme.

18) Besides bilateral and multilateral treaty arrangements some investment protection is afforded by general international law. Traditional international law provides a certain minimum standard for the treatment of foreigners and in this context poses certain conditions with respect to nationalisation. In case of violation of these rules, the national State of the injured part has the right to exercise diplomatic protection on behalf of its citizen, and take action against the injuring State. The principle of minimum standard has been under attack in recent years and the notion of diplomatic protection is contested since long by Latin American States. These States try to exclude diplomatic protection by the so called Calvo clause, a provision whereby the investor vis-à-vis the host Government takes the engagement not to seek the diplomatic protection of his home

Government. Since under traditional international law the right to diplomatic protection is a right of the State, it is contested that the Calvo clause can effectively deprive the home State of this right.

4) The applicable law

19) One of the key issues raised in the context of foreign investment is the issue of the applicable law. The particularities of the problem resides in the fact that the relationship concerned is one between a State and a foreign private party. There are abundant writings on the subject and many legal authors and scientific organizations have dealt with it, but much controversy remains.

20) Most aspects, if not all, of the activities of a foreign investor in the host country are governed, according to general principles of private international law, by the laws of this country, i.e. th host country's laws on taxation, on conducting business affairs, labour laws, monetary and customs regulations, etc. This is true whether or not the host Government and the foreign investor have concluded a contract setting out the terms of the investment ("investment contract") - unless, of course, this contract expressly provides for the application of a different law.

21) But the contracts between the Government and the foreign investor generally provide for a balance of rights and obligations between the parties and often contain engagements of the Government with respect to the very same laws which govern the investor's activity in the country; the

Government may provide for a favourable tax treatment or for import facilities or it may simply undertake not to modify the existing legislation to the detriment of the foreign investor. Now, if the investment contract itself, i.e. the contract containing these undertakings of the Government is subject to the law of the host country, the problem arises that the Government may, at its discretion, modify this law and thereby affect unilaterally its contractual rights and obligations.

22) In order to exclude this danger, many investment contracts make the contract subject to another legal order. A number of solutions have been found: the law of another country, principles common to the host country and the investor's home country, general principles of law, principles of international law or international law as such. In such a general form, these provisions must appear as impractical or, in any event, excessive since a number of aspects of the investor's activity in the host country are, as a matter of course, governed by the law of the host country. In order to overcome the dilema, a tendency is gaining ground which distinguishes between the law from which mutual contractual obligations derive their binding force, and the law which governs the material content of the contractual relationships. Such distinction would allow to base the binding force of the contract on a law which cannot be modified by either of the parties to the contract. Such a clause would make it acceptable to subject the interpretation of the contract and the entire activity of the investor in the host country to the law of the latter, since this law can no longer be

arbitrarily modified to the detriment of the investor.

23) But this concept according to which the law from which the contract derives its binding force and the law applicable to the contractual relationship itself are not necessarily identical is far from being universally accepted. The debate still or again, centers around the question whether the investment contract may be governed by any other law than that of the host country.

24) For a long time, especially in the years after the Second World War, legal authors on the issue of foreign investments, were primarily or even exclusively preoccupied with the protection of the rights of the investor. The interests of the host State which under certain circumstances may require a modification of the contract were often treated marginally. The investment contract itself frequently was considered as something absolutely fixed - some authors even referred to the "sanctity of contracts", overlooking that practically every legal system provides for the abrogation or modification of contract under certain exceptional circumstances.

25) Moreover, some legal writers insisted that such investment contracts were concluded on a level of equality between the Government and the foreign party. This may be correct if one looks at the power position and the economic strength of the two parties to the contract - in many cases the foreign company may have been more powerful and economically stronger than the contracting

Government. But this position of equality overlooks the fact that a Government is not simply an economic entreprise but bears responsibilities for an entire social community and therefore should be granted the right to modify under certain conditions and within certain limits a contractual relationship if the social welfare so requires.

26) The rigorous positions frequently adopted by investors and many lawyers may have been one of the causes for a recent development in the attitude of the developing countries with respect to investment contracts in particular in the field of natural resources. The position adopted now by the developing countries and expressed in the General Assembly Resolutions on Permanent Sovereignty over Natural Resources, on the Establishment of a New Economic Order and in the Charter of Economic Rights and Duty of States, seems to imply that the State is not bound by any obligation vis-à-vis an investor and can freely abrogate, as it seems fit, any contractual obligation.

27) Both positions described above - that of absolute sanctity of the investment contract and that of the discretionary power of the State to abrogate or modify its contracts - must appear as excessive and to the detriment of orderly international relations. It seems appropriate that the international community make an effort to define the limits within which the State is bound by its contractual obligations and in doing so take into account the general social responsibility of the State as well as the need for a minimum amount of security in contractual relations.

B. Industrialization contracts

28) While investment contracts still appear to be almost exclusively limited to relations between a party in a Western industrialized country, on the one hand, and a Government or public authority of a developing country on the other hand, industrialization contracts, as defined above, deal with all sorts of industrial relations : the sale of equipment, even on a turn-key basis, the provision of know how and technical assistance management and marketing agreements occur in contracts between two private corporations just as they occur in East-West and North-South economic relations.

1) Particularities of industrialization contracts

29) Contracts between firms from Western industrialized countries and a developing party, have a number of particularities ,some of which are similar to those encountered in the East-West trade:

30) a) The transaction often is concluded in the framework of an intergovernmental agreement. Such intergovernmental agreements either provide means for financing the project or simply set a mechanism which bilateral transactions between the States in question are to follow.

31) b) The corporation in the industrialized country frequently has as its contracting partner the Government or a public corporation. This raises particular problems with respect to the law applicable to the contract,and with respect to jurisdiction.(sovereign immunity).

32) c) In the framework of the above mentioned intergovernmental agreements, or simply as a part of export promotion by the industrial firm,, many

of the industrialization contracts with developing parties benefit from some special treatment with respect to export credits and insurance of export risks. Such contracts, which one may call "sponsored" contracts, are subject to more or less careful examination by the competent authorities in the country of the industrial firm. This examination may extend to the conditions and terms of the contract and to the viability of the project as well as to the capacity of the firm itself to meet its obligations.

33) d) While one may assume that in contractual relationships between industrial firms a certain equality in dealings exists even between firms of different sizes and economic strength, the situation is quite different in contracts between an industrial firm and a developing party , One of the criteria of underdevelopment is precisely the lack of sufficient numbers of specialists in technical as well as in the managerial field. For this reason, in many cases, the developing party will be at a disadvantage when it comes to evaluating the conditions of a contract (with respect to quality, terms for remunerations, guarantees, and qualification of the contracting party) and when it has to ascertain whether the other party properly performs its obligations.

2. The applicable law

34) When providing for the applicable law, the parties to an industialization contract generally do not have quite the same preoccupations than is the case with the parties to an investment contract. The foreign investor who provides in an investment contract for the application of a law other than that of the host country, is preoccupied primarily by the "stabilization" of the terms of his investment on which he agreed with the Government of the host country. This "stabilization" element, of course, also plays a role in industrialization contracts; but in these contracts the choice of law clause has additionally a very important function in determining the material content of the respective obligations of the parties. The law which the parties chose to govern their contract is not only to ensure that the parties (and in particular the Government) remain bound by their contractual obligations but also provides the rules for interpreting the contract and to determine the obligations of the parties where the contract is mute.

35) Of course, often parties to an industrialization contrac go through great pains to specify in detail the rights and obligations of the parties. But even very detailed contracts cannot treat exhaustively all possible situations that may arise, so that the designation of the substantive law governing the contract remains important. For this reason the parties to an industriali zation contract have an interest to have their relationship governed by an advanced legal system providing sufficiently developed rules in the field of contracts and related matters. Public international law still must be considered as rather rudimentary in many aspects; in spite of some recent tendencies it may

still be sufficient to ensure the "stabilization" effect in investment contracts, but it is hardly adequate to provide substantive rules to govern such complex matters as those which are the object of industrialization contracts. For the latter type of contract a municipal law or the system which has been referred to as the "lex mercatoria" (see below paragraph 41) must appear to be more adequate.

36) With respect to the choice of the governing law it can be said that the right of private parties in international commercial contracts to choose the law applicable to their contractual relationship (party autonomy) is widely recognized. Generally each party tries to have its own law applied to the contract since this law is more familiar to it, but also because one party often mistrusts the legal sytem of the other party.

37) This apprehension which parties to commercial transactions have with respect to the legal system and sometimes even more so with respect to the courts of their contracting party frequently does not have a very rational basis. In fact it is often the consequence of the limited outlook of some lawyers who find it difficult to appreciate the different approaches adopted by other legal systems. The greater the geographical and cultural difference, the more difficult it is for these lawyers to objectively appreciate the value of another legal system.

38) A consequence of this often rather irrational approach to issues of choice of law and jurisdiction, is the fact that quite frequently the forum and the applicable law are chosen for their "neutrality" rather than for their substantive content. Of course, objectively, the meaning of the term "neutrality" applied to the courts of a country is different from that applied to a given legal system. In fact, one may question whether the term "neutral law" in this context has any meaning at all. But in practice the parties often do not even distinguish between jurisdiction and applicable law and they somehow seem to feel that not only the judge of a third country is "neutral" but also his national legal system. This preoccupation with "neutrality" is so important that often the parties choose the law of a third country or provide for the jurisdiction of a third country's courts or arbitration in a third country, not because this law is particularly appropriate or just, nor because this judicial system is particularly efficient or the arbitration laws are especially conducive for a rapid and just settlement of the dispute, but simply because these laws or such jurisdiction are considered "neutral". In fact, it happens not unfrequently that the parties choose a "neutral" law of which they do not know the content, or that they choose the jurisdiction of the Courts of a country of which they do not even know the laws of procedure or of organisation of the judiciary, or that they provide for arbitration in a country of which they do not know the arbitration law and under regulations which are not familiar to them.

39) But there is some sort of justice in this rather arbitrary choice of law and jurisdiction because it is likely that in case of dispute, both parties

to acquaint themselves with the law and procedure of this third country and determine how it effects their position. Unsatisfactory as such a situation may appear, it is perhaps preferable to a situation in which one party acts on the familiar grounds of its own legal system while only the other party has to acquaint itself with a very different system.

40) But there is another disadvantage to the choice of national legal systems, whether "neutral" or not, to govern complicated international commercial or industrial contracts. In fact, national legal systems provide in their substantive rules primarily for situations of internal commercial relations. The particularities and specific requirements of international commercial relations are often disregarded.

41) For this reason, the parties to these international commercial relations have developed to an increasing degree specific rules of their contractual relations. Some of these rules have taken the form of commercial customs, others are reflected in agreements among members of a specific trade or in general conditions of contract, and some have even found their way into international conventions, or similar documents. One may note therefore, on the international level a growing body of substantive law applicable to international commercial relations. This body of law has been referred to by some authors as the "lex mercatoria" and receives increasing attention.

42) When it comes to contracts with developing countries, the question of the applicable law often appears to play an even more important role than is the case

in contracts between private parties, even if in some cases for lack of agreement no specific provision is made. Many developing countries insist, with a varying degree of emphasis, on the application of their own law. The reasons for this are similar to those for which an industrial firm insists on the application of its own law : their law is more familiar to them and one distrusts the law of the other party To these reasons should be added that some Governments still feel that it is below their dignity or even legally impossible that they submit a contract with a foreign private party to a law other than their own. In some countries there are even express legal provisions to this effect.

43) When the issue of choice of law in industrialization contracts is examined, two additional aspects should be taken into consideration : first of all, the foreign party hesitates to agree to the law of the developing party, in particular if this party is the Government itself, for fear that this law may be changed to its disadvantage. We have referred to these considerations when dealing with the "stabilization" aspect of the choice of law clause. Another aspect which should be considered when it comes to the choice of law, is again the aspect of underdevelopment : as pointed out above, even the legal systems of industrialized countries are not specially modelled for the needs of international commercial relations; but many of them have reacted to the particular circumstances of industrial activities on the national level. It may therefore be assumed that the legislator in the industrialized countries has made an attempt to adequately respond to the specific problems arising in industrial activities. The legislator in developing countries will have had much less occasion to deal

with these specific problems. Thus it would appear that for the time being, the law of industrialized countries responds more adequately to the specific problems arising in the field of industrialization in general and industrial cooperation particularly.

44) But this advantage is only relative. In fact, the choice of the law of an industrialized country may be satisfactory with respect to solving particular aspects of industrial contracts, but it may not be sufficient to take into account the international aspects in general and the specific aspects due to the fact that one of the party is the Government or the national of a developing country. In fact, at present, it is not likely that any given legal system, whether in industrialized countries or in developing countries, replies to the full range of the needs which the law governing industrialization contracts with developing contracts should meet.

45) In an attempt to overcome these deficiencies, UNIDO and other international organizations have prepared manuals and give advice for the careful preparation of contractual documents. But the general conditions of contract, model agreements and similar documents which these manuals propose for application by developing countries have almost exclusively been elaborated in the industrialized countries and in any event hardly provide for the particular situations due to development problems. Reference is often made to documents of professional organizations like FIDIC or FIBTP *), as well as to documents prepared in the framework of the United Nations Economic Commission for Europe and originally oriented for

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*) Fédération Internationale des Ingénieurs-Conseils, Fédération Internationale du Bâtiment et des Travaux Publics

East-West Trade. These documents are now applied also in contracts with developing countries although the situation is quite different : While in East-West trade both parties with respect ot information available and managerial and technical infra-structure may be assumed to negociate on an equal footing, the problems of underdevelopment with which the developing party has to cope puts this party at a true disadvantage. The documents and assistance provided to developing countries in this respect, aim at reducing or even overcoming this disadvantage, but they do not seem to provide legal provisions which take into account the present situation of imbalance and provide the necessary redress.

IV. JURISDICTION AND SETTLEMENT OF DISPUTES

A. Causes for dispute

46) Before examining the methods for settling disputes, arising in industrial cooperation, it may be of interest to examine how such disputes arise. It is suggested to distinguish three different causes for disputes in industrial cooperation:

47) a) During or after performance of the contract, the parties may disagree with respect to the interpretation of a specific clause of their contract or with respect to the appreciation of certain facts and their consequences. It often occurs that the contract of the parties is insufficient either because the parties have not thought of a particular aspect of their cooperation or they expressed themselves in an ambiguous or contradictory manner. It may also occur that certain facts are in dispute, such as the

conformity of a piece of work to contractual standards. If disputes are of this nature, the parties in general will have an interest in settling them as rapidly as possible and avoid that their cooperation suffers from a prolonged dispute. In practice, most of these disputes are solved amicably, either in negotiation or through a third party functioning as an expert or a conciliator. It is important for the parties to avoid that their difference of view with respect to a particular issue degenerates into litigation and thereby causes more harm to the project, to the cooperation and to the parties than either of them may gain even in case of winning the dispute. American businessmen express their attitude in this respect by saying "a bad compromise is better than a good lawsuit".

48) b) The situation may be different if the dispute finds its cause in a change of the equilibrium of the contractual relations. In fact, the circumstances under which the project is carried out may have changed in such a manner that one of the parties has no longer an economic interest in performing the contract or even looses by such performance. A change may have occurred in the price of raw materials or in the price which may be obtained for the product, it may have occurred in the requirements of the market, in transport conditions or in a number of other circumstances. In the absence of legal or contractual provisions whereby the conditions of the contract may be adapted to such fundamental changes of circumstances, the party for which the performance of the contract has become onerous, may be tempted to provoke a dispute and seek a pretext for witholding performance of its obligations until the

other party consents to a modification of the terms. In order to avoid such situations, contracts often provide adaptation clauses. The most frequent of these clauses are the price revision clauses which provide for adaptation of the contract price once the factors which, at the time of the agreement, had determined this price have changed; often a detailed formula for this adaptation is spelled out. In recent times, a more general formula seems to have become more widely accepted : an increasing number of contracts seem to contain what is called a "hardship clause". To some extent these clauses express a principle found in many legal systems, referred to as the "clausula rebus sic stantibus" according to which a contract is concluded under the reservation that no fundamental change occurs in the circumstances prevailing at its conclusion.

49) In general, a fundamental change in circumstances affects only one party to the contract or at least affects one party considerably more seriously than the other; in other words, one party has a vital interest in reaching an agreement on adapting the contract to the change of circumstances, whereas the other party does not have such an interest. Of course, the other party, in the interest of future good collaboration or for other reasons may be willing to make some concessions, but in many cases this will not be so. In other words, it is important that the contract which provides for an adaptation in case of change in circumstances, grants to a third party powers to determine how the contract is to be adapted. If such a possibility for the adaptation of the contract by a third party exists, the party not being affected

by the change in circumstances may be much more willing to agree to a negotiated solution and may not wish to take the risk that in the end the adaptation is determined by a third party. In any event, the adaptation of the terms of the contract to modified circumstances depends for its effectiveness to a large extent on the powers of a third party to equitably set out the new terms.

50) c) Finally, disputes may be caused by circumstances that do not affect the economic equilibrium of the contract, but which nevertheless affect the willingness of one of the parties to perform its obligations: the management or the corporate policy of one of the parties may have changed (in some aspects this may be comparable to a change in the Government of the other party), a party having obtained what it expected from the contract may have lost interest in meeting its corresponding obligations (e.g. for reasons of liquidity or interest rates, it may economically be more interesting to assume the costs of a time-consuming lawsuit rather than paying a debt immediately) or it may be that the personal relations between the parties have deteriorated to an extent that a proper performance of the mutual obligations is no longer possible in view of a climate of antagonism and distrust.

51) Of course the refractory party in most of these situations is in bad faith, but this bad faith is not always evident for an outsider : the more complex a factual and legal situation is, the more easily a plausible pretext may be found.

In situations of this sort, conciliation seems to be bound to fail and a rapid and efficient procedure should be available for the enforcement of contractual obligations. On the other hand, the rapidity and efficiency of the procedure should not be at the expense of justice and equity: without having given both parties a chance of presenting their claim and their evidence and without careful examination of the respective argument, it is hardly possible to say whether a claim or argument is frivolous or well-founded. Thus minimum conditions of an equitable procedure have to be observed even in case of apparently frivolous claims or defenses.

B. Forms of dispute settlement

52) The explanations as to the causes of disputes may have shown that the most appropriate method for the settlement of a dispute depends on the nature, the causes and the circumstances of the dispute. These forms of settlement may be divided in five groups :

1) Negotiations among the parties

53) It would appear on first sight quite natural for the parties, in case of a dispute, to meet for negotiations. Thus, further explanations on the subject and, in particular, special provisions in the contract may seem superfluous. In practice, the situation is more complicated.

54) Once a difference of opinion among the parties arises, one of them or both have to make concessions. But the persons conducting the negotiations are not always in a position or willing to make such concessions; this may be due to a number of causes and may occur in particular in cases where the

person conducting the negotiations fears that he may be held responsible for the situation which gave rise to the dispute; when he informs his superiors it is possible that he is more preoccupied with defending his own position rather than setting out the facts in an objective manner. The superior who has to make a decision with respect to what concessions are to be made will have difficulties in reaching a correct decision.

55) For this reason it is important that the negotiation for settling a dispute should be conducted at a relatively high level already at an early stage and before the parties have taken entrenched positions which they may find difficult to abandon without losing face.

56) Many contracts of industrial cooperation provide that parties should make an attempt at a negotiated settlement prior to having recourse to a third-party form of settlement. But few contracts seem to be sufficiently precise with respect to this clause and in practice the contractual provision obliging the parties to negotiate prior to having recourse to other forms of dispute settlement does not seem to play an important role. It may be useful to examine the question of how the parties may provide already in their contract for efficient methods of solving the dispute by negotiation.

2) <u>Third-party intervention without a decision (conciliation, mediation, good offices, etc.)</u>

57) Where the parties have an objective interest in a rapid settlement of the dispute or in a continuation

of the good relationship, the intervention of a third party may often be very useful in pointing out to them the weaknesses of their respective positions and in helping them to overcome the psychological obstacle which often prevents them from making a compromise. There are other situations, especially the ones pointed out above under IV A. (3) where attempts at conciliation are nothing but a waste of time.

58) Efficient conciliation requires first of all a conciliator who has sufficient knowledge of the substance matter in order to seize the true causes of the dispute. Furthermore, it takes diplomatic gifts and a considerable amount of imagination to find, together with the parties, a solution which both parties are ready to accept by their own free will. The conciliator should be briefed as to the particularities of the dispute, but such briefing should not be too extensive in order to avoid that too much time is lost in conciliation. It is important for the success of conciliation that each party - facing the conciliator alone or in the presence of the opponent party - may speak freely before the conciliator and envisage with him all sorts of solutions; therefore, rules of conciliation generally provide that the parties in a later litigation are not bound by declarations made before or during the conciliation proceedings and that the conciliator may not sit later as an arbitrator.

59) Should the conciliation fail, it may be useful to provide that the conciliator, together with the parties, draws up at least a statement of the points of disagreement, so that the later litigation is clearly circumscribed; in fact, precise terms of reference may speed up considerably any litigation.

3) Third party finding without binding force (expert's opinion etc.)

60) As pointed out above under IV A. (1), one of the reasons for disputes is the difference in the appreciation of certain facts. Such differences often require a rapid decision. Especially in cases of contracts for construction and operation of industrial projects, where a delayed decision on the disputed facts may cause the entire project to be held up. In such a case, the parties may refer to an expert who decides as rapidly as possible the point in issue, but the parties reserve the right not to accept this decision. If the parties do not accept the expert's decision they will have to submit the entire dispute to third-party settlement, in particular to arbitration. Of course this could mean a loss of valuable time and considerable delay in carrying out the project. For this reason, contracts often provide that the decision of the expert has at least a provisionally binding force, that is to say the project has to continue according to the expert's decision, even if the parties do not agree to it, and request settlement of the dispute by arbitration. In that event, the arbitral tribunal is not bound by the expert's decision; it may reach a different finding and if the expert's instructions may not be reversed any more, it may have to award damages. A number of model contracts provide for such expert's decision and FIDIC as well as ICC have elaborated rules for their intervention.

61) In theory, any person knowledgeable in the substance matter of the dispute may be entrusted with the role of the expert. In practice however, the parties, in order to ensure that the decision is rendered rapidly, appoint as their expert someone already familiar with the project : contracts for construction work of civil engineering, for setting up factories or for similar

projects, provide that the owner is assisted by an independent engineer who supervises for the owner the work of the contractor. It is generally this engineer whom the parties entrust with the function of the expert in settling their disputes. Although the engineer is generally an independent firm, he is appointed by the owner and the contractor may therefore not always find him an objective third-party. This is one of the reasons why, as pointed out above, the decision of the engineer may be questioned and in that event has only a provisionally binding force.

4. Binding decision by a third party appointed by the parties to the dispute (arbitration, decision by a referee)

(a) Arbitration

62) In the field of commercial relations, arbitration is a very frequently applied form of settling disputes. A number of reasons are invoked when it comes to justifying recourse to arbitration rather than to ordinary courts : expeditiousness and confidentiality of proceedings, competence of arbitrators, the confidence of the parties in the arbitral tribunal and sometimes even the question of costs.

63) With respect to disputes on the national level, the advantages of arbitration are perhaps not as evident as some may think. But on the international level, in the field of international commercial relations in general and cases of industrial cooperation in particular, arbitration has a very important role to play.

(i) Competence of arbitrators :

64) Arbitrators are not necessarily better qualified than the judges of ordinary courts, especially in countries which provide in their judicial system special chambers for commercial affairs; and in fact one finds not unfrequently judges sitting in on arbitral tribunals.

65) Nevertheless, the chances that the members of an arbitral tribunal are better qualified than the courts to decide a particular case are greater since they are chosen in function of the specific dispute which is submitted to them. In the case of the ordinary courts, the choice of the judge who is to hear the case depends on a number of heterogeneous factors such as the domicile of the debtor or the location of the debtor's assets, repartition of functions within the court and sometimes even such criteria as the first letter of the claimant's or the defendant's name. Arbitrators, on the other hand, are in principle chosen in function of the specific case which they are to decide and parties to important international disputes generally select their arbitrators with careful attention. Chances therefore are quite high that an arbitral tribunal is particularly well qualified to decide the case for which it has been set up.

66) In international commercial disputes the specific qualification of the arbitrators do not relate only to technical aspects but also to the specific legal problems of international commercial relations. In other words, arbitrators in such cases have to be familiar not only with the practices of international commercial relations and with the "lex mercatoria", but also with the principles of several legal systems and with international law. It is therefore only understandable that international commercial arbitration is the domain of a relatively small circle of specialists in the field.

(ii) Expeditiousness :

67) If one bears in mind that arbitration proceedings may last for several years and if one thinks of the possibilities of appeals to ordinary courts which the arbitration laws of most countries provide at least for exceptional circumstances, one can hardly say that arbitration proceedings necessarily are more expeditious.

68) In practice, much depends on the circumstances, on the complexity of the case and on the specific rules of arbitration applied in the case. Some institutional arbitration proceedings, especially those at the commodity exchanges, may settle disputes within a matter of days or at most within a few weeks. Other procedures, especially those which provide for the exchange of one or several briefs may take much longer. Additional problems arise when the arbitrators are important personalities living in different countries who find it difficult to concert their schedules for the meetings of the arbitral tribunal. In fact, it often occurs in international arbitration cases that several or all arbitrators as well as the parties and their counsel have to travel to the place of the hearing.

69) Because of these and other practical difficulties arbitration proceedings are not always as expeditious as the parties or at least the claimant may wish them to be. Expeditiousness therefore is perhaps not the most important reason for parties to an international dispute to have recourse to arbitration. In any event, it should be noted that the existence of an arbitration clause

often eliminates controversies over jurisdictional issues which may account for considerable complications in international disputes.

(iii) Costs of arbitration proceedings :

70) Here again it is difficult to generalize, since much depends on the individual case and especially on the arbitration institution to which the dispute is referred and on the procedure applied. But one may say that the high degree of specialization of those participating in international arbitration tends to render the proceedings as such more expensive than ordinary court proceedings. However, these costs may be more than compensated for by the advantages drawn from the fact that the dispute between the parties may be resolved in one single procedure rather than being fought out in a number of different national courts of different levels.

(iv) Confidence of the parties in the arbitral tribunal due to their participation in the process of setting it up :

71) It is in fact an essential aspect of arbitration proceedings that the parties have the right to participate in setting up the tribunal and in many cases it may be this right which determines parties to provide for a settlement of disputes by arbitration.

72) The parties may either be free in their choice of the arbitrators or restricted by a pannel from

which the arbitrators are chosen or by the qualifications which the arbitrators have to meet. Especially in cases where the parties freely choose their arbitrator, a privileged relationship often exists between a party or its counsel and the arbitrator appointed by it. Such privileged relationship may in fact facilitate proceedings since it may help counsel to address himself to those aspects of procedure which are of particular interest to the arbitration tribunal.(It should be noted that contrary to the Anglo-Saxon judicial tradition, some judicial proceedings, e.g. in France, provide very little communication between the courts and the parties and the courts generally do not indicate the items with respect to which they wish to hear argument - this tradition often reflects on arbitration proceedings before arbitrators formed in French or similar traditions).

73) But the privileged relationship between an arbitrator and the party having appointed him may also have a very negative effect in case the arbitrator considers himself simply as the advocate of "his" party. This is by no means always the case, but when it occurs, the other arbitrators, and in particular the president of the arbitral tribunal, have to pay particular attention to conduct proceedings in an impartial manner.

74) In disputes related to industrial cooperation, the question of confidence in the third party by which the dispute is settled plays a particular role in international arbitration. In fact, already

among private parties of different nationalities there is a certain amount of mistrust with respect to the courts of the other party. This apprehension is increased when the other party is a Government because sometimes the contracting party of the Government feels, rightly or wrongly, that the courts have difficulties in finding against their own Government, especially if it stands against a foreign party. For this reason, international commercial contracts often provide a neutral jurisdiction, sometimes the court of a third country but more often arbitration. The advantage of arbitration is seen in the fact that the parties have the possibility to participate in setting up the tribunal and that this tribunal often sits in a neutral country and frequently settles the dispute in applying legal provisions which do not derive from the national law of either party.

75) It has been pointed out above that the fears which determine a party to an international contract to reject the law of the other party and the jurisdiction of the other party's courts often is based more on psychological than on legal reasons, and the choice of a "neutral" law or a "neutral" jurisdiction is made not always on a very rational basis. But where contracts with Governments are concerned, the situation is different. Governments are in a position to modify their own law and they may attempt to give instructions to their own courts or set aside the decisions of these courts. It is only prudent of the private contracting party to try and protect itself against such possibilities

and it would appear wise to do so even if - as, in all likelihood, it is normally the case - there is no particular indication that the contracting Government has in the past or intends in the future to gain an advantage by changing the law or influencing the courts. A provision for dispute settlement by international arbitration avoids any possible apprehension and thereby creates confidence not only in the third party deciding a possible dispute but, moreover, it brings an additional element of trust and confidence in the contractual relations of the parties themselves.

(v) The private nature of proceedings :

76) Insofar as the private nature of arbitration proceedings is concerned, it appears certain that the parties themselves consider in many cases such privacy as one of the major advantages of arbitration proceedings in commercial matters. Generally it is not good for a businessman's reputation to be involved in litigation and if he really has to litigate, the less people who know about it, the better. This is true also in the case of Governments which often have perhaps even less of an interest than private companies to have the dispute in which they are involved be known to the general public. Moreover, a dispute may relate to a defective performance by one of the parties and, of course, this party would not like others to know of it. And finally industrial and commercial secrets are better protected if a dispute is settled in confidential arbitration rather than in public court hearings.

77) One of the disadvantages of this private nature resides in the fact that the legal principles applied by the arbitrators often are not known to others than the parties, so that even very carefully reasoned arbitral awards do not contribute to the formation of law which takes place through commercial practice and judicial decisions. This deficiency is beginning to be remedied to some extent since in recent times, arbitral awards are more frequently published, especially in versions which are abridged so as to prevent identification of the parties. In particular the ICC seems to have changed a long standing tradition of secrecy and proceeds with the publication of extracts from arbitration awards.

78) The private nature of arbitration proceedings has another more serious aspect : it gives the parties the possibility to have at least some sort of enforcement of even those contractual provisions which are contrary to mandatory rules of national law or public policy. In theory at least, even disputes over illegal agreements could be submitted to some sort of arbitration. Of course, when one of the parties appeals to State courts against such an award or where a party has to seek the assistance of State authorities to enforce it, the considerations of public policy prevail.

79) But in certain cases, the parties may not dare to address themselves to the courts or may have no interest in doing so; this is true in particular in cases where contractual obligations violate anti-trust regulations, taxation or currency laws, etc. There are cases known where arbitrators were willing to apply against the contract of the parties mandatory rules of national law (or in one case, at least, the anti-trust law of the EEC). But it may well be

that in other cases, arbitrators upheld otherwise illegal contracts.

80) This consequence of the confidential nature of arbitration proceedings is something against which no complete remedy seems to exist, since it appears hardly possible to prevent two persons from addressing themselves to a third person for the settlement of their dispute over an illegal matter. However, what is important in this context is that an award obtained in such a fashion will not be enforced by the State authorities and a recourse may be had against it before the State courts.

(vi) The applicable law :

81) State courts determine according to their own municipal law - more precisely, according to the national rules of conflict of laws - which law is applicable to the substance of the dispute. Thus the court of one State may come to the conclusion that, under its own rules of conflict of laws, it has to apply the substantive law of another

State in order to decide the dispute brought before it. The rules of conflict of laws of most States allow the parties to international commercial contracts to choose the substantive law which is to govern their contract. In fact, the parties to such contracts have almost complete freedom to choose any system of law to govern their contract - as long as this system is a national system of law. The issue becomes controversial when the parties want to choose international law, general principles of law or something like the body of rules to which we referred as "lex mercatoria" (above, No. 41). State courts may hesitate or even refuse to recognize and put into effect such a choice of law clause.

82) The situation is different before an arbitral tribunal. It is still controversial how an arbitral tribunal has to determine which conflict of law rules it applies; but there seems to be little doubt among legal writers that an international arbitral tribunal may apply international law, general principles of law, the lex mercatoria, etc. In practice, many arbitral tribunals have in fact applied various systems of law and did not consider themselves bound to apply the municipal law of a State. Moreover, it should be noted that the Washington Convention on the Settlement of Investment Disputes of 1965 expressly provides that the arbitral tribunal may apply "such rules of international law as may be applicable" (art. 42 paragraph 1).

83) This greater flexibility in the choice of the applicable law, besides being of interest to parties to the dispute, attributes to arbitration proceedings a particularly important role in the development of the international law of contracts in general and of investment and industrialization contracts in particular.

(vii) Enforcement of the award :

84) Finally, an advantage specific to international arbitration should be mentioned - the enforcement of the award. Once the arbitrator has decided the dispute, the parties know what to do. But they not always act accordingly. The sanctions for not complying with the terms of an award vary according to the context in which the award was rendered. The award of an arbitral tribunal set up in the context of the professional organization of a small group of businessmen, such as the arbitral tribunals set up at most of the international commodity exchanges, in most cases is scrupulously observed since the member of the association who does not live up to the terms of the award is likely to be excluded from the association or at least he will be ostracized.

85) In circumstances where no such social sanctions are provided, the party seeking enforcement of the award will have to have recourse to the authority of the State for enforcement of the award. If the award was rendered in the same country, the enforcement of it is generally granted under the local laws on arbitration and enforcement. When we come to enforcement abroad, the situation becomes more complicated. The courts of some States give effect to foreign awards by providing them with the exequatur or by at least treating them as an agreement among the parties which may be enforced in ordinary court proceedings. But the normal enforcement of a foreign award, i.e. immediate seizure of assets of the debtor is generally granted only if the State where enforcement is sought has bound itself by an international treaty to grant such enforcement.

86) A great number of bilateral treaties have been concluded among States but the most important treaties in this respect are the Convention on the Execution of Foreign Arbitral Awards signed in Geneva on September 26, 1927 (Geneva Convention) and the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards signed in New York on June 10, 1958 (The New York Convention). Practically all industrialized States including all the members of the CMEA and a considerable number of developing countries, have ratified the New York Convention. As a consequence, an arbitral award generally can be enforced abroad more easily and more rapidly than is the case with a judgment of a national court.

87) In principle, the New York Convention is applicable to a foreign award no matter where it has been rendered, but an important number of contracting States have availed themselves of the possibility to restrict application to awards rendered in another contracting State. But the application of the convention is not limited to nationals of the contracting States.

88) Therefore the developing countries which have not ratified the New York Convention and their nationals may seek enforcement of an award rendered in a contracting State against an industrial firm while the awards against themselves can be enforced only with difficulty, if at all.

(viii) The arbitration clause as a means to prevent disputes :

89) Finally, it should be pointed out that the arbitration clause as such may have a beneficial effect in dispute settlement. The parties know that a procedure exists whereby the parties can have their dispute decided by a body in the objectivity and competence of which they may have confidence. This fact alone may induce the parties to a certain moderation in their negotiations for dispute settlement. If one party takes an unjustified position and is intransigent , the other may have recourse to the arbitral tribunal to have its rights protected. Thus the usefulness and importance of arbitration in international commercial relations should be judged not only by the manner in which international disputes were settled

in arbitration proceedings, but also by the disputes which were avoided due to the existence of an arbitration clause.

90) In summing up, it may be said that in international commercial relations, arbitration is the form of settlement of disputes which is far preferred, especially for reasons of confidence in the arbitral tribunal, for flexibility in the application of substantive law, for the private nature of the proceedings and for facilities in enforcing the award.

(b) Decision by a referee

91) During the last few years, specialists in international commercial relations have paid particular attention to a problem which seems to become of increasing importance : international contracts, and especially industrialization contracts, often are extremely complex and have to be performed over a long period of time. The parties, when negotiating and concluding their contract, in such complex cases can hardly provide for all possible situations which may occur. This may be so either because the situation is so complex or a certain future event is so unlikely that the parties have omitted to provide for them; or it may be that the parties have thought of the event but did not have all the elements available. A good example for the latter case can be seen in a long term delivery contract where the parties want to determine the price for future deliveries according to certain criteria but do not yet know the elements of fact necessary to

apply such criteria (e.g. future price for certain raw materials, for labour and transportation, etc.) and may not be able to work out a formula which allows automatic determination of the price once the elements of fact are known. In all these cases the contract has "gaps".

92) It has been suggested by a number of authors that such gaps may very well be filled by an arbitral tribunal. On the other hand, one may be of the opinion that filling a gap is not really the task of an arbitrator because it does not require the interpretation or the application of the parties' agreement but rather the making of a new agreement, at least a partially new agreement. The third party which equitably fixes the price of a product which the parties to the contract were not yet able to fix, in completing the contract with respect to an essential element, assumes the position of the parties rather than that of a judge or an arbitrator. For this reason it has been suggested that such gaps in the long term contracts should be filled by special procedures before what has been called a "referee". Some specialized arbitration institutions provide already for such procedures, especially with respect to determining price or quality. On a more general level proceedings before a referee have been suggested at the Stockholm Conference of the International Bar Association in August 1976. It will have to be seen to what extent this rather new institution of the "referee" will be accepted in practice.

5) Decision by the courts

93) Although, as pointed out above, arbitration is generally preferred for the settlement of international commercial disputes, for a number of reasons, recourse to courts cannot be excluded - provided, of course, the State party may not claim sovereign immunity.

94) First of all, international commercial arbitration generally remains subject at least in some aspects to the national arbitration laws of the country where the arbitration takes place. These national arbitration laws to a varying degree provide for the intervention of the ordinary courts : the courts may be called upon to pronounce themselves on certain issues of law (this is the case in particular in the English system), or they may have powers to revise, under certain circumstances, the arbitral award.

95) Moreover, there are certain types of remedies which are reserved to the ordinary courts. This is the case in particular with respect to provisional measures which a party may seek pending proceedings on the merits. These provisional measures frequently require immediate enforcement (e.g. sale of perishable goods, seizure of an object in dispute, etc.); therefore they are generally reserved for the ordinary courts.

96) There is also a number of subject matters which are reserved for the courts : thus some countries provide that disputes with respect to patent rights

are subject to the exclusive jurisdiction of the ordinary courts and cannot be brought to arbitration.

97) But, of course, the most important field in which the courts have to intervene are those cases where the parties have not been able to agree on an arbitration clause. In that event, the aggrieved party has hardly any other remedy but to bring the case before an ordinary court. Often the aggrieved party has a choice of a number of different jurisdictions. Generally, for the above-mentioned psychological reasons, each party would prefer to have the tribunal of its own country decide the dispute; however, a party may also have an interest in bringing the case before the tribunal of the country where the assets of the debtor are located because this will considerably facilitate the enforcement of a judgement which it may have obtained.

C. Procedures and institutions for the settlement of disputes

98) Proceedings for settlement of disputes which do not lead to a binding decision by a third party frequently do not follow a pre-established procedure. Some arbitration institutions provide for conciliation according to rules set out in special regulations; but apparently such procedures are not very frequently used.

99) Court proceedings, of course, follow the laws set up by each State and the parties may have a choice only insofar as they could agree to submit the dispute to the courts of one country rather than to those of another. The procedures for hearing commercial cases vary considerably from one country to another but they are necessarily marked by a certain formalism.

100) One of the particularities of arbitration proceedings lies in the fact that these proceedings generally are much less formal or formalistic than proceedings before national courts. Nevertheless in arbitration, too , a certain number of rules are necessary in order to provide for orderly proceedings and a fair hearing of the case.

101) With respect to arbitration proceedings, one has to distinguish between ad hoc arbitration and institutional arbitration.

102) In the case of ad hoc arbitration, the setting up of the tribunal is determined by the parties alone, and the procedure to be followed by the tribunal is determined again by the parties or by the tribunal which they have set up.

103) Since it may occur that the parties, after having agreed on arbitration in principle, do not reach agreement with respect to their arbitrators, even ad hoc arbitration has to provide for an institution which appoints one or several arbitrators in case the parties fail to do so or in case the arbitrators appointed by the parties do not reach agreement as to the president of the arbitral tribunal or the umpire.

104) For this purpose, the parties may grant the power of appointment to the president of a national tribunal, to a chamber of commerce, to the President of the International Court of Justice, or to quite a number of other judicial or commercial institutions.

105) Moreover, the freedom of the parties to set up the tribunal and determine proceedure is generally also limited by national laws on arbitration especially those of the country where the arbitral tribunal has its seat. These laws generally provide for rules to be applied.

if the parties have not specified the rules of procedure and they contain certain fundamental rules which the parties and the tribunal cannot set aside.

106) In the case of institutional arbitration, the parties refer the dispute to a pre-established body which assists them in setting up the tribunal and which provides the rules of procedure Although many of the presently available rules of procedure are linked with a specific arbitration institution, some arbitration rules apply only to ad hoc arbitration.

107) This is the case in particular with the UNCITRAL-Rules as well as the ECE-and the ECAFE-Rules.

108) Arbitration institutions are quite numerous; for instance the list of institutions exercising an activity in the field of internatinnal commercial arbitration edited in 1958 by the U.N. Economic Commission for Europe, mentions not less than 113 institutions.

109) Many of these arbitration institutions are related to commercial associations on a national or international level. Quite a number of the professional associations, especially in the field of commodity trade, and their arbitration institutions are located in London.

110) Among the national institutions of a general nature, special mention should be made of the Courts of Arbitration set up by the London Chamber of Commerce and the Corporation of the City of London , the arbitral tribunal of the Zurich Chamber of Commerce and of the Stockholm Chamber of Commerce, the Arbitration Chamber of Paris and the Court of Arbitration of the Austrian Chamber of Commerce in Vienna.

111) But the most active of the national arbitration associations seems to be the American Arbitration Association which is said to provide for some 15 000 arbitration proceedings every year.

112) Among the national arbitration institutions special mention has to be made of the Foreign Trade Arbitration Commissions of the Chambers of Commerce and Industry of the member-countries of the CMEA.

113) Perhaps the most important international arbitration institution is the Court of Arbitration of the International Chamber of Commerce in Paris. This institution is of particular relevance for commercial disputes in Western Europe, but disputes in East-West Trade and disputes from contracts between parties in Europe and developing countries are also referred to it.

114) Specialised in some important aspects of industrial cooperation, the International Center for Investments Disputes (ICSID), set up under the Washington Convention for the Settlement of Investment Disputes between States and Nationals of Other States of 1965, is particularly relevant for the present subject.

115) By February 1977, Washington Convention had been ratified by 67 states, industrialized and developed. The Latin American States, the Socialist States (with the exception of Roumania and Yougoslavia), several Arab States, some Asian States (in particular India) and Australia have not ratified the Convention.

116) All of these institutions provide, in varying degrees, assistance to the parties in setting up the Tribunal and in the conduct of proceedings. Many of these institutions have a list of arbitrators or panels and in some cases, in particular in arbitrations before the Foreign Trade Arbitration

Commissions of the CMEA countries, these lists are binding so that the parties may not choose any arbitrators outside the panel. The proceedings, especially those before professional associations, are often quite informal and sometimes very rapid; other rules of procedure are much more detailed or even formalistic and procedural debates are not always excluded.

117) Most of the above mentioned arbitration institutions and procedures are used primarily in commercial disputes between private companies or between a private party and a Government or a State Corporation. But there should be no difficulty to use these or similar institutions and procedures for the settlement of commercial disputes between State corporations. In fact, a great majority of cases brought before the Foreign Trade Arbitration Commissions of the CMEA countries are disputes among State corporations of these countries. And even when it comes to settling purely commercial disputes between Governments, one may also consider the use of one or the other of the above mentioned institutions and procedures, rather then of procedures for dispute settlement under general public international law - just as the Permanent Court of International Arbitration under the Hague Conventions (originally meant to be used exclusively for disputes among States) has been adapted so as to also hear cases where one of the parties is not a State.

V. SUBJECTS FOR FURTHER INVESTIGATIONS AND FUTURE ACTION

A. In the field of foreign investment

118) In the present situation the issue of foreign investment is extremely controversial and perhaps the subject on which it may be most difficult to reach a consensus, as has been shown for instance by the recent failure of an attempt of the International Law Association to agree on a model investment contract which could have been suggested to parties desiring to enter into such a contract.

119) Taking stock of the present situation with respect to foreign investment may be a useful exercise and show the true scope of the problems. A number of national and international institutions have been concerned with the two opposing aspects of foreign investment (i.e. national control over foreign investment and investment protection); it may be useful to confer to one or several of them the work to be conducted in this context. However, the problem seems to be that, in view of interests at stake and the often very antagonistic positions adopted, special attention is necessary to ensure that the issues are examined free of pre-conceived ideas and without ideological undertones.

120) Once the present situation with respect to the two main aspects of foreign investment has been investigated, and presented in this manner, it may become more clear in which fields further progress is desirable and possible.

121) Since a satisfactory solution of the outstanding problems requires that the interests of both parties are adequately taken into consideration, the problems of foreign investment and their solution should be approached simultaneously from the aspect of national control over foreign investment and investment protection. It would appear that better progress can be made by promoting solutions which take both aspects into account instead of dealing with each aspect separately, as it has been done too often in the past.

122) In this context, one may examine how existing bilateral and multilateral schemes for investment protection may be linked with the action by the host country to integrate foreign investment into its national development policy and how the home country of the investor may contribute to these efforts of the host country. But in any event, it should not be forgotten, that the foreign investment is only a means to an end i.e. the promotion of the economic and industrial development of the host country. Investment protection and national control over foreign investment should be seen in this perspective.

123) It may be of interest to pay particular attention to joint-venture regulations by which the host Government attempts to gain some control over the activities of foreign corporations. How to provide the mechanisms for control and supervision without disturbing the proper functioning of the firm ? How to avoid deadlocks in the management of the firm once the Government and the

foreign corporation associated in the joint venture have opposing views on an issue ? In fact both partners have other interests besides the proper functioning of the firm : the Government has to assure objectives of a general nature relevant to the country as a whole and the foreign corporation has its own general objectives of a group of companies in which a particular joint venture may only be one of many operations. Between these interests the specific interests of the firm, jointly owned by the Government and the foreign corporation may be neglected. It may be worthwhile to examine how problems of this nature may be overcome, possibly by introducing a third partner such as an international development bank as equity shareholder or by introducing local private parties or national, foreign or international investment funds as additional shareholders.

124) Another aspect of foreign investment which may deserve further attention is the question of investment incentives, provided for in particular by the capital importing countries: Are any of these incentives really effective in attracting foreign investment to the country and, if yes, what is the price? Besides the economic effects of such investment incentives, it may be of interest to find adequate means whereby the host Government may ensure that the investor benefiting from the incentives really makes the contribution to national development which was expected and for which the incentives were granted. Moreover, the legal and administrative problems may be examined which arise from the fact that numerous derogations from the generally applicable legislation are made in favour of foreign corporations. It may also be of interest to examine how to avoid excessive competition among developing countries wishing to attract foreign investment.

125) Such investigations would have to be conducted on a theoretical and on a practical level with national administrations as well as with foreign investors. In fact, a number of such investigations have already been carried out and it would, as a first step, be useful to compare their results and determine where further research is necessary.

126) In the field of investment protection UNIDO, perhaps together with ICSID or the World Bank itself may wish to examine whether previous attempts at multilateral investment protection or investment insurance deserve to be further pursued.

B. <u>In the field of industrialization contracts</u>

127) Industrialization contracts seem to have provoked much less heated debates and fewer proposals than was the case with foreign investment. In this field, the approach seems to be more oriented by the practical needs of drafting of contracts and their performance. In fact, it may be useful that the joint study stresses this practical aspect in the field of industrialization contracts.

128) First of all, it may be useful to investigate the present contractual practice with respect to the different types of industrial cooperation contracts. Some work is done already especially by way of empiric studies of certain clauses in such contracts.

129) This investigation should not only cover the different types of contracts and specific clauses thereof (e.g. "force majeure" - clauses, hardship clauses, guarantees etc.) but also the possibilities to link up and interrelate several distinct contracts relevant to the same project e.g. the sale of a factory on a turn-key basis and the agreement for the marketing of its products.

130) Once the factual situation with respect to the contractual practice has been established, it would be useful to examine this practice in order to :

131) a) determine to what extent this practice takes into consideration the specific requirements of the developing countries,

b) examine what forms of standardization are possible.

132) It would appear that the question of standardization is one of the legal issues in which the joint study could make a particularly valuable contribution. It is submitted that such standardization could make a serious contribution to facilitate contract negotiation by providing a uniform framework in which the particularities of each contractual relationship could be spelled out much more easily.

133) Contrary to the party from the developing country, the party from the industrialized country often has a number of specialists at its disposal to cope with complicated situations. Any simplification in contract negotiation would therefore be of a particular benefit to the former. It should be examined whether this standardization should take place on a national level - i.e. each developing country spells out (perhaps with the help of UNIDO) the binding rules applicable to industrialisation contracts - or whether international standardiz-

ation is preferable. Of course standardization on a national level is to be more easily achieved and a number of aspects (such as public bids, procurement etc) are already provided for in several national legislations, but standardization on an international level would have the advantage of also facilitating communication and cooperation among developing countries themselves.

134) It will then have to be seen whether a standardization can lead into something like a code for the law of industrialization contracts. Such a code could embody the progress already achieved in certain sectors by institutions like Uncitral or other public and private institutions for the harmonisation of commercial law. Particular reference should be made to the work presently undertaken in this field by Uncitral, the UNECE, the Unidroit, the Afro-Asian Legal Consultative Committee and other bodies. In drawing up this code, a particular effort should be made to render it comprehensible to those who have to use it. This code by no means should be a text which only few specialised lawyers understand. The people responsible, e.g. economists in an a ministry of development and industrialization should be able to read and interpret the code just as well as the engineer or representatives of the foreign firm.

135) Of course, the elaboration of such a code of industrialization contracts would be a very ambitious project and it is by no means certain it can be realized.

136) In any event there seems to be little chance that such a code be adopted in the form of an international convention. It may be much more practical to provide it as an instrument to which the parties may choose to refer when they determine the law applicable to their contractual relationship.

137) With respect to practical measures of a more immediate nature, one may envisage action on three levels :

a) to develop a regular service for advice and assistance to negotiators in developing countries: Documentation and information on the contracting firm and its competitors; assistance with respect to the technical, economic and legal specifications of the project and the drafting of the contractual documents in order to ensure that the contracts properly protect the interests of the developing party and provide all necessary guarantees. It may be interesting to examine the usefulness of a task-force on which a developing country could draw in case of need.

b) to provide training for lawyers, especially from developping countries, to acquaint them with the complicated field of industrialization contracts, especially with respect to drafting such contracts, supervising their performance and conduct proceedings for the settlement of disputes which may arise out of them.

c) to favour the bilateral cooperation among States. In particular, industrialized states should provide for easy access to the the institutions for information and assistance in their countries. A central institution in each industrialized country, to receive and channel requests for information and assistance, may be of great help for planners in developing countries.

C. <u>In the field of settlement of disputes</u>

138) In this field too, it may be useful to investigate into the present situation and determine in particular to what extent, the presently existing forms of dispute settlement are used, for what reasons, and how they may be ameliorated.

139) Thereafter, it would appear that the following measures may be promoted :

140) It may be useful to examine what steps can be taken in order to facilitate and promote <u>conciliation</u> proceedings. In fact

it would appear that a considerable contribution to rapid and efficient dispute settlement would be made by setting up a Center which could make available, without many formalities and on short notice, an experienced and knowledgeable conciliator. It may be preferable that, in setting up the list of conciliators, the Center does not have to follow binding proposals of outside institutions but may establish itself this list on the sole basis of the personal qualifications of the conciliator.

141) A similar form of assitance may be provided in the field of expert opinions. One may think either of a Center supplying experts in case of need or of some sort of supervision over the qualification of experts or over their decisions in particular cases.

142) With respect to arbitration it has already been pointed out that international commercial arbitration in general and arbitration of disputes in industrial cooperation is the domain of a relatively small group of specialists. These specialists are almost exclusively from developed countries, either from market or centrally planned economies. As a consequence, it often occurs that in arbitration proceedings to which a developing country is a party, no national of a developing country participates - neither as arbitrator nor even as counsel.

143) This seems to be due not only to the fact that developing countries in general suffer from a lack of specialists. In fact it would appear that the legal profession is, at least in certain developing countries, among those branches in which the lack of specialists is least acute. But there seems to be little interest in acquiring the theoretical basis and the practical experience in the very particular branch of law with which the specialists in international arbitration deal.

144) The problem of communication may also play an important role. In any event it would seem most important to promote among the lawyers of developing countries knowledge of, and interest in international arbitration proceedings. In fact, arbitration is important not only for the settlement of disputes between parties from developing countries and industrialized countries, but also among parties from developing countries especially when they come from different legal systems. In order to promote such experience and interest, better communications are of great importance. In a field in which the confidential aspect plays such an important role as in arbitration, personal contact among the specialists is of particular importance. This personal communication should be promoted among lawyers of developing countries who are interested in arbitration questions but also between these lawyers and the specialists in the industrialized countries. Some arbitration institutions, especially ICSID but also the ICC have undertaken efforts in order to promote this contact and awareness but there is still a lot to be done.

145) It will have to be seen whether a growing interest in arbitration by lawyers from developing countries will lead to new institutions for dispute settlement. If one looks at the impressive number of existing arbitration institutions one would feel at first sight that there is no need for such new institutions; but it has to be seen whether the existing arbitration institutions really meet the needs and pre-occupations of developing countries or whether they can be adapted to meet them. In fact, with the exception of ICSID and the Foreign Trade Arbitration Commissions of the CMEA countries, the existing arbitration institutions are primarily oriented to private commercial relations.

146) They were not set up to deal with the specific problems arising in the cooperation between private parties and governments or state corporations.

147) The Foreign Trade Arbitration Commissions of the CMEA countries therefore may be specially adapted to meet the specific problems in industrialization contracts. Judging from the practice of these Arbitration Commissions, it appears that they are particularly well aware of the requirements of centrally planned economies and of the specific problems which arise when contracts with foreign private parties have to be integrated into the planning process. But, of course, the restrictions with respect to the choice of arbitrators may be an obstacle to a more wide spread use of these institutions in industrialization contracts.

148) In fact, as pointed out above, the most important feature in arbitration remains the method of determining the arbitrators and the choice available to the parties. In this context, the arbitration institution has a very critical role to play when it comes to appointing the president of the arbitral tribunal or the umpire in case the parties or the arbitrators appointed by them fail to agree on such a president or umpire.

149) The fact that the Court of Arbitration of the ICC as well as the Foreign Trade Arbitration Commissions in the CMEA countries are closely associated with institutions which certainly are not ideologically neutral i.e. the International Chamber of Commerce on the one hand, and the National Chambers of Commerce in the CMEA countries on the other hand, makes it doubtful whether either of the two institutions will inspire the confidence which is necessary for a further promotion of arbitration as a mode of settlement of disputes in industrial cooperation.

150) Other institutions will have to be examined in order to determine the extent to which they meet the needs of arbitration in industrial cooperation. ICSID, for example, is limited by its terms of reference spelled out in the Washington Convention. This Convention applies only to investment disputes and to nationals of contracting states. ICSID presently seems to be willing to enlarge its scope but it has to be seen to what extent this will be practical.

151) Whether an existing institution can be adapted to meet the needs of industrial cooperation or whether it appears preferable to set up a new institution, it would seem tempting to provide a link between the above-mentioned code of industrialization contracts with this arbitration institution. In fact, it would seem that such a code would best be administered by an arbitration institution rather than by national courts which may have difficulties in integrating it into their national legal systems.

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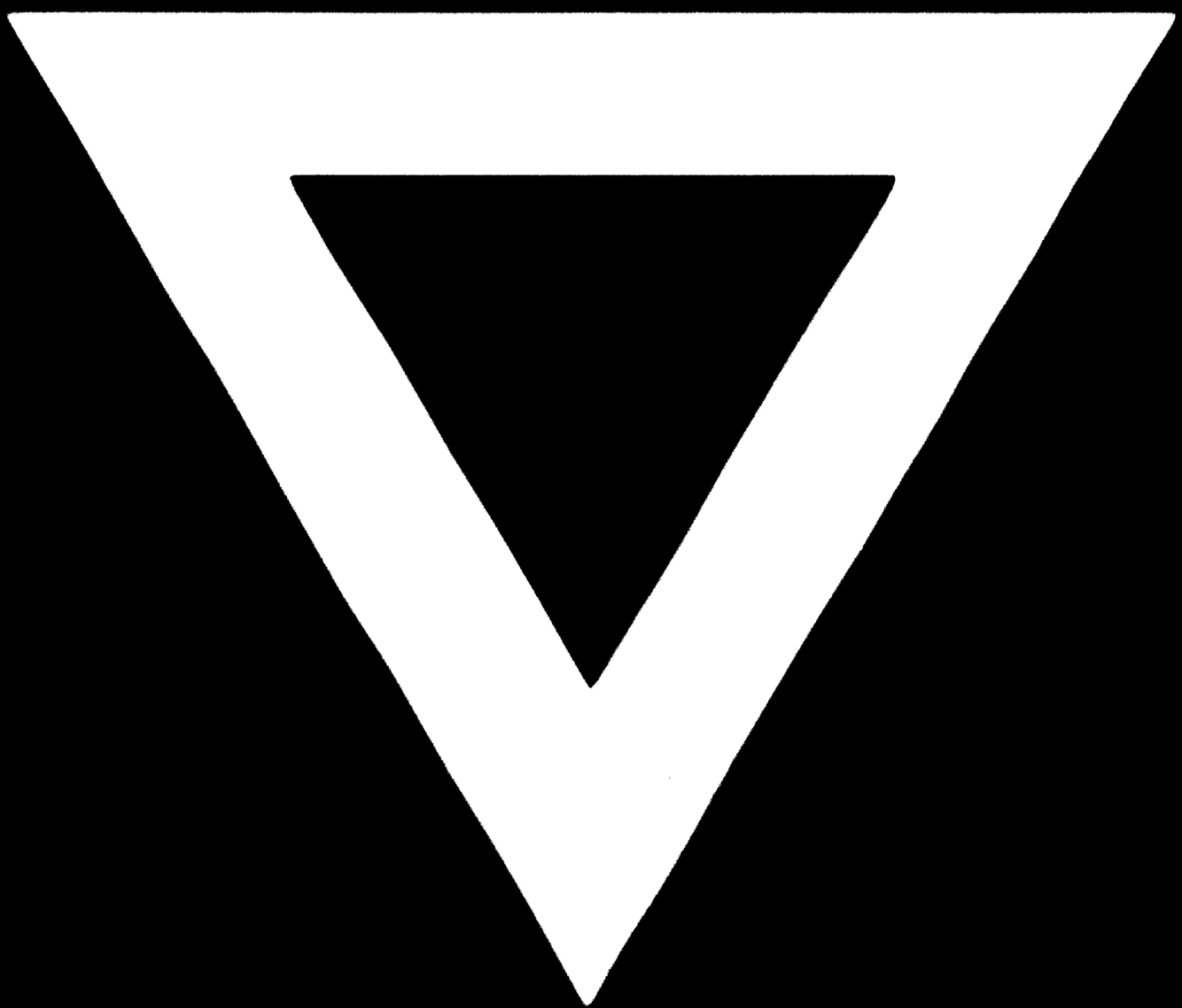

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