The Advancement of International Law

Charles Leben

FRENCH STUDIES IN INTERNATIONAL LAW

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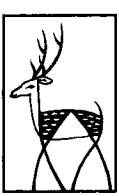

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Part 1

Advances in the Techniques of International Law

1

State Contracts and their Governing Law: A Reappraisal*

OF ALL THE areas in which the advancement of international law has been implicated in the second half of the twentieth century, that of contracts made by states with private persons is probably among those where the stakes have been highest and the controversies keenest. This type of legal relation has raised at least two separate but not unrelated categories of question: that of sovereign immunities of states and that of what are called 'state contracts'. As regards the former, the substantial change undergone by international law with the abandonment of the theory of absolute immunity and the adoption of the theory of restrictive immunity is barely contested any longer and questions arise only over quite how to determine restrictive immunity.[1] As regards state contracts, however, and despite considerable doctrine on the matter, no general consensus seems to have arisen yet, as evidenced by the polemics that very regularly recur.[2] These polemics are invariably

* First published as 'Retour sur la notion de contrat d'Etat et sur le droit applicable à celui-ci' in *Mélanges offerts au Professeur H Thierry: l'évolution du droit international* (Paris, Pedone, 1998) 247. For a more detailed study of my position see C Leben, 'La théorie du contrat d'Etat et l'évolution du droit international des investissements' (2003) 302 *Recueil des Cours de l'Académie de Droit International de La Haye* 197.

[1] For a recent review see M Cosnard, *La soumission des Etats aux tribunaux internes face à la théorie des immunités de l'Etat* (Paris, Pedone, 1996); I Pingel-Lenuzza, *Les immunités des Etats en droit international* (Brussels, Bruylant, 1998); G Hafner, M Kohen and S Breau (eds), *La pratique des Etats concernant les immunités* (Leiden, Martinus Nijhoff, 2006); H Fox, *The Law of State Immunity* 2nd edn (Oxford, Oxford University Press, 2008).

[2] See one of the last papers of RB Lillich, 'The Law Governing Disputes under Economic Development Agreements: Reexamining the Concept of Internationalization' in RB Lillich and CN Brower (eds), *International Arbitration in the 21st Century: Towards 'Judicialization' and Uniformity?* (New York, Transnational Publishers, 1994). Lillich discusses Bowett's refusal to accept that international law and the general principles of law apply to economic development agreements. See DW Bowett, 'State Contracts with

about the relevance of public international law for governing this type of contract. It appears obvious that the divergences arise essentially from contemporary conceptions of public international law, of its subjects, of the relations it may govern and of its possible advancement compared—on all these points—with a 'classical' scheme of things that prevailed at least until about 1945. It is a distinctly 'evolutionist' view that is to be defended here, both because my basic postulate is that international law, like all law, is liable to evolve with the 'society' of which it is an expression, and because it can be shown that observation of international practice confirms this position.

This study, as said, does not concern a new domain but on the contrary a domain that has been very largely explored by legal scholarship and especially French-language doctrine.[3] Within this doctrine, studies by Prosper Weil and Pierre Mayer stand as major mileposts in understanding state contracts.[4] But far from being convergent, their work is contradictory. And yet, without engaging here in any scholastic endeavour to harmonise the opinions of

Aliens: Contemporary Developments on Compensation for Termination or Breach' (1998) 59 *British Yearbook of International Law* 49, 51; AFM Maniruzzaman, 'State Contracts in Contemporary International Law: Monist versus Dualist Theories' (2001) 12(2) *European Journal of International Law* 309; M Kamto, 'La notion de contrat d'Etat: une contribution au débat' (2003) 3 *Revue de l'Arbitrage* 719. At the time of writing I was unaware of L Lankarani El-Zein, *Les contrats d'Etat à l'épreuve du droit international* (Brussels, Bruylant, éd de l'Université de Bruxelles, 2001). It contains pointed criticism of doctrinal positions seeking to connect state contracts with the international legal order.

[3] For a general bibliography on state contracts see NG Ziadé, 'References on State Contracts' (1988) 1 *ICSID Review* 212; E Paasivirta, *Participation of States in International Contracts and Arbitral Disputes* (Helsinki, Lakimiesliiton Kustannus, 1990); C Leben, 'La théorie du contrat d'Etat et l'évolution du droit international des investissements' (2003) 302 *Recueil des Cours de l'Académie de Droit International de La Haye* 197.

[4] See especially P Weil, 'Problèmes relatifs aux contrats passés entre un Etat et un particulier' (1969-III) 128 *Recueil des Cours de l'Académie de Droit International de La Haye* 101; 'Droit international et contrats d'Etat' in *Mélanges offerts à Paul Reuter* (Paris, Pedone, 1981) 549; 'Les clauses de stabilisation ou d'intangibilité insérées dans les accords de développement économique' in *Mélanges offerts à Charles Rousseau* (Paris, Pedone, 1974) 301; 'Principes généraux de droit et contrats d'Etat' in *Le droit des relations économiques internationales. Etudes offertes à B Goldman* (Paris, Litec, 1982) 387 and his general lectures at The Hague, 'Le droit international en quête de son identité' (1992-VI) 237 *Recueil des Cours de l'Académie de Droit International de La Haye* 95. Weil's writings on state contracts, except for his 1969 Hague lectures, are now collected in *Ecrits de droit international* (Paris, PUF, 2000) 303. For P Mayer see 'Le mythe de "l'ordre juridique de base" (ou *Grundlegung*)' in *Le droit des relations économiques internationales. Etudes offertes à Berthold Goldman* (Paris, Litec, 1982) 199 and 'La neutralisation du pouvoir normatif de l'Etat' (1986) *Journal du Droit International* 5.

'authorities', it does seem possible to defend the idea that while Mayer's definition of state contracts provides the sound conceptual basis the theory was lacking, it does not exclude but on the contrary supports Weil's major insight that such contracts are subject to public international law. State contracts can be conceived of as new acts of international law. Such a claim encounters strong objections that will require close examination.

State Contracts As New International Legal Acts

State Contracts as Contracts entered into by States as Subjects of Public International Law

Growing Awareness of a New Category of Contracts made by States

The first observation to be made concerns the historical dimension of the subject. One cannot understand the hesitations of arbitration tribunals and the diversity of scholarly opinion unless one allows for the fact that what was to be apprehended was a phenomenon that had appeared in a recent period and that was evolving at the same time as the first attempts were being made to systematise it. The main arbitration awards that commentators were to reason on in diagnosing the emergence of a new category of contracts related to petroleum concessions in the Middle East in the 1950s and 1960s.[5] The Libyan awards (*Texaco, Liamco, BP*) and the *Aminoil* award, not to mention the expansion of ICSID (International Centre for Settlement of Investment Disputes) case law, came after the first major studies by Mann, Verdross, Wengler and Weil, to name but a few.[6] Those commentators, then, were working on a still unestablished practice and with minimum historical hindsight relative to a phenomenon that was only just emerging.

[5] See G Cohen-Jonathan, *Les concessions en droit international public* (Thèse, University of Paris, 1966).

[6] FA Mann, *Studies in International Law* (Oxford, Clarendon Press, 1973); A Verdross, 'Quasi-international Agreements and International Economic Transactions' (1964) 18 *Yearbook of World Affairs* 230; W Wengler, 'Les accords entre Etats et entreprises étrangères sont-ils des traités de droit international?' (1972) *Revue Générale de Droit International Public* 313. On the Libyan awards see B Stern, 'Trois arbitrages, un même problème, trois solutions: les nationalisations pétrolières libyennes devant l'arbitrage international' (1980) *Revue de l'Arbitrage* 3. On the Aminoil award see P Kahn, 'Contrats d'Etat et nationalisation. Les apports de la sentence arbitrale du 24 mars 1982' (1982) 109 *Journal du Droit International* 844; G Burdeau, 'Droit international et contrats d'Etats. La sentence *Aminoil c. Koweit* du 24 mars 1982' (1982) *Annuaire Français de Droit International* 454.

While almost all of these scholars agreed that the practice seemed to produce contracts that were neither municipal law contracts nor international contracts such as are made between private persons, just as they acknowledged that not all contracts between a state and a private person are 'state contracts', they were hard pressed to come up with a purely legal criterion by which to differentiate 'state contracts' and ordinary contracts entered into by states.

State contracts are generally investment contracts, but that does not mean that all investment contracts are state contracts nor that there cannot be any state contracts outside the domain of investments (Mann's paper, which seems to have coined the expression 'state contracts' was about international borrowing).[7] These contracts contain references, in various forms, to public international law. But Mann had defended the idea as early as 1944 that the principle of freedom of contract allowed a state and a private person to adopt public international law as the law applicable to a contract between them on the basis of private international law techniques.[8]

State contracts have also been spoken of as economic development agreements,[9] without there being any objective criterion to say when and under what circumstances an investment contract could be so characterised. Even the most elaborate conception of the notion, that provided by Weil, does not escape this criticism. In distinguishing *internationalised contracts*—whose basic legal order is municipal law and whose proper law is international law—from *contracts in international law*—whose basic legal order and proper law are both international law—he characterises state contracts as having 'their centre of gravity . . . in the international orbit'. He adds 'that it is not all state contracts that should be considered thus to appertain to the international legal order but only those of them that are actually integrated by objective legal or politico-economic ties into relations

[7] FA Mann, 'The Law Governing State Contracts' (1944) 21 *British Yearbook of International Law* 11 reprinted in *Studies in International Law* (Oxford, Clarendon Press, 1973). In the same area see also G Delaume, 'Des stipulations de droit applicable dans les accords de prêt et de développement économique' (1968) *Journal du Droit International* 336.

[8] Mann, 'State Contracts', *ibid*, 190–91. He added though: 'In absence of an express reference a State contract should be regarded as internationalized, if it is so rooted in international law as to render it impossible to assume that the parties intended to be governed by a national system of law' (at 194). He cited the example of the obligations subscribed by Germany on the basis of the Young Plan for payment of reparations provided for by the Treaty of Versailles.

[9] See JN Hyde, 'Economic Development Agreements' (1962) 105 *Recueil des Cours de l'Académie de Droit International de La Haye* 266; SI Pogany, 'Economic Development Agreements' (1992) 7 *ICSID Review* 1.

between states, that is essentially—but not exclusively—economic development agreements or investment contracts'.[10]

But Weil himself recognised that 'this distinction between ordinary state contracts and state contracts with an international basis defies any objective and readily understandable criterion'.[11] Moreover, it rests on a further distinction between the basic legal order of the contract (*Grundlegung*) and the law governing the contract—a distinction that was to come in for some radical criticism.[12]

State Contracts as presented by Mayer

Mayer's essential contribution was to provide a purely legal criterion for distinguishing contracts entered into by states from *state contracts* in the strict sense of the term. The former are made *within the state's*

[10] Weil, 'Droit international et contrats d'Etat' (n 4) 580. It would have been hard to find an example corresponding more closely to the criterion of a contract that, through objective ties, was part and parcel of relations between states than the various contracts in the Eurodif affair: in February 1974 the Finance Ministers of France (V Giscard d'Estaing) and Iran signed a framework agreement in Paris on Franco-Iranian cooperation. France was to construct five of Iran's 25 nuclear power stations, supply enriched uranium, build a gas liquefaction plant, a steel-making complex, etc. In June 1974 during an official visit to France, the Shah of Iran signed a cooperation agreement with the French Government for the peaceful use of nuclear power. In December 1974 French Prime Minister Chirac signed a new agreement in Teheran specifying the scope of cooperation of the two countries in nuclear matters. The agreement provided, among many other things, for the formation of a French company, Sofidif, 60% owned by France's Commissariat à l'énergie atomique (CEA) and 40% owned by Iran's Atomic Energy Organisation. Subsequently the CEA was to transfer 25% of its shareholding in Eurodif (a company producing enriched uranium) to Sofidif, so indirectly allowing Iran a stake in the company. Various conventions were entered into between Sofidif and Eurodif that were governed by French law with an ICC arbitration clause. The agreement also provided for a $1 million loan from the Iranian government to France's CEA, the agreement being governed by Iranian law with an ICC arbitration clause. Besides the loan to the CEA, Iran made another $943 million loan to Eurodif in an agreement of July 1977. The agreement was governed by Iranian law with an ICC arbitration clause. Out of the mass of litigation that was to follow the Iranian revolution and last 12 years nothing need be said other than that when one aspect of the affair came before France's Cour de cassation, Advocate-General Gulphe noted: 'we are on the borderline between private international law and public international law and one may wonder whether these agreements should come under one or the other' (Cas. civ. 14 mars 1984, JCP 1984, II, 20205, concl. Gulphe, note Synvet); see also B Ancel and Y Lequette, *Grands arrêts de la jurisprudence française de droit international privé* 2nd edn (Paris, Sirey, 1992) 514. And yet the entire dispute, both in the arbitration tribunals and in the French courts, was treated as a private law matter with municipal law applying. This clearly shows that it is not being a part of relations between states through objective ties of a politico-economic order that transforms a contract made by a state with foreign persons into a state contract but solely legal criteria by which it can be recognised that the contract was made by the state as a subject of international law.

[11] Weil, 'Droit international et contrats d'Etat' (n 4) 581.

[12] Mayer, 'L'ordre juridique de base' (n 4).

legal order and with the state as it stands in its legal order, that is the state as administration, while the latter are made by the state as a subject of public international law *within a legal order external to the state*. The recognition of state contracts *stricto sensu* involves purely legal criteria: the inclusion of an arbitration clause, neutralisation of the state's normative power by the addition of clauses stabilising the law of the state, if applicable, possible inclusion of the contract in a treaty of international law and under certain circumstances, internationalisation of the governing law.[13]

However, for reasons we shall return to, Mayer refuses to consider that this external order governing contracts entered into by states as subjects of international law with private persons might be the legal order of public international law. Instead, he presents a sophisticated revamped version of the theory of the *contrat sans loi*. This second part of Mayer's theoretical construction is highly paradoxical and not very convincing. However, it seems more logical to infer from the fact that in a state contract it is the state as a subject of international law that is contracting, that the legal order within which the contract is made is indeed that of public international law. But this means admitting that international law may have evolved to allow a new category of legal acts—state contracts—to arise. This did not occur overnight but is the result of a historical process that led certain contracts made by states with private persons to be shifted from the orbit of municipal law (including its rules on conflict of laws) to the orbit of international law.

State Contracts as Contracts governed by the International Legal Order

The paradoxical character of what is announced here is obvious enough: the contracts generally in question (mostly investment contracts) are international contracts in the sense of private international law with a governing law clause that may refer to international law or to its general principles but that very often designates the contracting state's national law as the governing law and sometimes contains no *electio juris* clause. Under such circumstances it is difficult to escape the reasoning of private international law even if it is complicated by introducing the distinction between basic legal order and governing law.

[13] Mayer, 'La neutralisation' (n 4) 29–39. See also the development of his thinking on this point (the analysis of what an international court is) that reinforces his general analysis of state contracts in 'Contract claims et clauses juridictionnelles des traités relatifs à la protection des investissements' (2009) *Journal du Droit International* 71, 86 and see below fn 60 and ch 4 (at 111).