



Thesis
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**Enforceability of Arbitral Awards Containing Interest - A Comparative
Study between *Sharia* Law and Positive Laws**

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Abstract

The dynamics of our globalised world open the way for international trade and transactions between different countries; this may lead to conflicts in laws where transactions and trade may be subject to different legal systems. One of the biggest issues in international commercial law is disputes over the charging of interest, for example with regard to late payment, interest-based loans, or compensation for damages. Interest disputes are considered to be a complex area of law and even more complex in the international field. At the international level, interest claims may be connected to many areas of commerce and thus governed by various laws, which are different from one country to another; moreover, each country has its own interest rate and such rates are changeable according to the nature of law and economics under some jurisdictions. Furthermore, the concept of interest itself is affected by influences such as religious beliefs and economic, political and cultural trends. Interest can be treated as a substantive or a procedural matter. The settlement of these disputes therefore faces difficulties.

Arbitration, as a method for settlement of disputes, is characterised by special features that assist in resolving these issues; but it faces some obstructions, especially in international commercial arbitration. The practices of arbitral tribunals and national courts in this regard are different. The results of different interpretations, approaches, and theories with regard to arbitration, at the pre-arbitration, during arbitration and post-arbitration stages, may also differ widely due to the diversity of financial and legal systems such as Common Law, Civil Law and the Islamic legal system – *Sharia* Law – across different countries. Each legal system has a different methodology and theories, even within an individual country under one legal system, and a state within a federal system has its own laws, which may have different interpretations in this respect.

The New York Convention of 1958 on enforcing foreign arbitral awards was established in favour of arbitral awards and for the purpose of unifying international rules of arbitration. This Convention provides some procedural and substantive rules for the enforcement of foreign arbitral awards, but also provides some grounds for refusal. These rules have been affected by different interpretations under different jurisdictions and legal systems, which lead to different perspectives on the matter of charging interest and settlement by arbitration. The outcome of applying the NYC under these interpretations often has the opposite of its intended effect: the rejection of foreign arbitral awards. Due to such ambiguities, courts occasionally intervene in arbitration in all its stages.

The interventions of national courts occur in three stages: enforcement of the arbitration agreement, enforcement of the contract under the applicable law to the agreement, and enforcement of the foreign arbitral award. The confusion between substantive and procedural

laws also creates confusion with respect to public policy, non-arbitrability and enforceability. In addition, there may be a lack of clarity on the scope of arbitration with respect to the parties' agreement, whether or not the parties have agreed to the interest rates and periods and whether or not they have agreed to the authority of the arbitrator. These issues affect the enforceability of an arbitration agreement, the law applicable to the disputed contract, the freedom of parties, the authority of the arbitrators and the enforceability of the awarded interest. The thesis studies how arbitral awards containing interest have been interpreted across the three aforementioned legal systems under the NYC 1958 in Saudi Arabia, Egypt, the UAE, England, France, and the US and the enforceability of such awards.

Attestation

I understand the nature of plagiarism, and I am aware of the University's policy on this. I hereby declare that no portion of the thesis is the work of others, and I clearly acknowledge that no part of the thesis has been submitted elsewhere in support of an application for another degree or qualification.

Signature Mohammad M Althabity

Date 29/01/2016

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Abbreviations

CISG	United Nations Convention on Contracts for the International Sale of Goods
NYC	The New York Convention 1958
(UN)	The United Nations (UN)
UNCITRAL	United Nations Commission on International Trade Law
FAA	The Federal Arbitration Act
ICC	The International Chamber of Commerce
ICSID	The International Centre for Settlement of Investment Disputes
WIPO	The World Intellectual Property Organization
PECL	The Principles of European Contract Law
UCC	The Uniform Commercial Code
AAA	The American Arbitration Association
LCIA	The London Court of International Arbitration
UCTA	The Unfair Contract Terms Act 1977
UTCCR	The Unfair Terms in Consumer Contracts Regulations 1999
UAE	United Arab of Emirates
U.S.	United States
GCC	The Gulf Cooperation Council
ILA	The International Law Association
SAMA	The Saudi Arabian Monetary Agency
<i>Sharia law</i>	A law based on the Islamic sources
<i>Riba</i>	Extra, charging illegal interest
<i>Gharar</i>	Uncertainty
<i>Fiqh'</i>	Islamic Jurisprudence
<i>Qiyas</i>	Analogy
<i>Ijtihad</i>	Human activity and independent judgment
<i>Ijma</i>	Consensus by collective reasoning by qualified scholars
<i>fa'ra</i>	New case
<i>a'sl</i>	Legal precedent
<i>Furu al Fiqh</i>	The second branch of Fiqh
<i>Usul al Fiqh</i>	The first branch of Fiqh
<i>Quran</i>	The Holy book of Islam
<i>Hadith</i>	The sayings and practices of the Prophet Muhammad
<i>Lex arbitri</i>	The law of the place where arbitration is to take place
<i>Lex contractus</i>	The law governing a contract
<i>lex fori</i>	The laws of a forum
<i>lex trans</i>	The transnational law
<i>usura</i>	Latin the word of use
<i>intereo</i>	To be lost
<i>Istihsan</i>	To consider something good
<i>Istidlal</i>	A method of juristic deduction not falling within the scope of analogy
<i>Istishab</i>	Islamic legal term for the presumption of continuity
<i>Il'lah</i>	The effective cause
<i>Majalla</i>	The Ottoman State' Legal Provisions
<i>Maqasid</i>	In harmony with reason
<i>Tahkeem</i>	Arbitration in Arabic
<i>Fatwa</i>	An Islamic ruling
<i>Ma'taoum</i>	Any eaten
<i>Althmnyah</i>	A value
<i>shart-jazai</i>	A penalty clause
<i>Asl</i>	Fundamentals
<i>Wasf</i>	Components
<i>Ijab</i>	The offer

qabul

Riba Al-Fadl

Riba Al-Nasih

Diwan Al-Mazalim

pacta sunt servanda

The *acceptance*

Fadl' means increasing or excess

Nasih' means delay, rescheduling or defer for an addition

The Board of Grievances

Latin – 'promises must be kept'

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Chapter 1. Introduction

Arbitration as a legal mechanism and one of the alternatives for the settlement of disputes between parties has become widely used. It is characterised by speed, convenience, low cost, and neutrality. The notion of international arbitration has evolved and progressed in the last few decades through changes in some arbitration laws and treaties, by establishing international organisations and conventions to overcome some obstacles, and by attention that it has received by researchers. So far, some dilemmas relating to the laws, interpretations, the understanding of the mechanism of arbitration and the authority of local courts, especially in international arbitration, may prevent it from achieving its purpose.

Trade and its methods have been developed and have created different types of contracts and transactions at the international and national levels. As a result, on account of globalisation, international trade and investment needs all have led to modern interest rates in modern practices and laws. Laws have been enacted in different jurisdictions to govern trade, whether national or international, but it is increasingly complex with regards to the international aspect. In fact, interest claims are related to loan, late payment, compensations for breach contracts and damages disputes. Interest is also involved in different industries such as banking disputes, contracts of sale of goods, services such as construction contracts etc., and investment disputes in general. It may be subject to different fields of law such as financial law, economic law and commercial law. Interest claims may be also subject to some international commercial laws or conventions, there may be conflicting between private international law and public international law in this regard.

Interest laws and the related disputes are the most complex issues in the international commercial arbitration, where every country has its own laws according to a legal system. In addition, some countries adopt a mixed law between two or more legal systems while other countries under a different legal system do not recognize legal systems or laws of another country, like *Sharia* law, as non-national law. Every legal system has several theories and rules with regards to contracts and interest. By contrast every law under each legal system has a different interpretation in the law cases, especially with regards to interest. Different legal systems play an important role in dealing with arbitration proceedings and the enforcement the foreign arbitral awards. Such role may be a negative or positive impact on arbitration. Many influences may produce negative impacts on this interpretation, such as religions, economic, financial systems and politic. The law of interest varies from one country to another according to these influences.

In most countries interest-based loan contracts are limited to the legal interest rates defined by usury laws. Interest rates are different from one country to another for loan contracts and usury; some countries set fourth either minimum or maximum interest rate or set both rates, and in some countries interest-based loans are forbidden. For example, interest rates could start

from 1% and go up to 20% or more depending on which country's laws would govern the loan contract. A violation of the maximum interest rate or the legal interest rate is considered a violation of substantive law or usury statutes in these countries. By contrast, a waiver of a legal right such as a minimum interest rate is considered violation of public policy in some countries. There are some fears over charging interest on loan contracts in some Islamic countries due to the concept of *Riba*, which is prohibited under Islam. These countries attempt to avoid such action, where Islamic banking is established. As an alternative to traditional banking, different types of interest-free Islamic contracts, for example *Murabaha*, are offered. In all Islamic countries, there are non-Islamic banks as well as Islamic ones, so some banks do practice *Riba*. However, there is a misunderstanding in the concept of *Riba* and the meaning beyond this concept even within Islamic countries.

There are many arguments with regards to the meaning of interest, usury and *Riba*, and a confusion regarding to the application of these concepts. Some jurisdictions gather loan and late payment claims in the same category due to the country's substantive laws. Other countries separate between loans and late payments, where each case takes a different legal concept and where interest on late payment issues may take the same legal effect as compensations for damages and breach of contract. These compensations in most countries are allowed under different approaches, where some countries require them to be equal to the actual damages, others leave such matter to the arbitrating parties or otherwise do not agree on the settlement of damages, and others do the same thing but stipulate the parties' agreement shall be reasonable. Most countries have different laws with regards to compound and simple interest, and with regards to the time period of the interest, whether pre-judgment or post judgement, from the breach or debt till the judgement or till the full sum price, amount and compensation has been paid. The interest laws in different countries often conflict with each other.

The influence various applicable laws may have on arbitration is especially acute in the issue of determining interest. Arbitral awards are influenced by the State in which the choice of law is made, the State of enforcement of foreign arbitral decisions, and the law of courts of the seat of arbitration in which the award is made. Additionally, there are some dilemmas facing arbitration in this regard, including the misinterpretation of the laws applicable to the dispute, arbitrability, and public policies. The impact of intervention of national courts on the freedom of parties and the power and the authority of the arbitral tribunal, which may conflict with the nature of arbitration in some aspects. In brief, the next sections will address the complexity of the issues regarding interest and arbitration with more clarification.

1.1 The complexity of the issues

1.1.1 *The impacts different legal systems may have on arbitration*

In this thesis, the legal systems can be limited to Common Law, Civil Law, an Islamic legal system or *Sharia* law, or a mixed legal system. They are different according to the sources of law, the method of relying on these sources, and the strength of these sources. The Common law was unwritten law and much of it determined by custom.¹ The law in this system 'stems not only from the legislative branch of government, but also, and more importantly, from the precedents established by higher courts'.² This system is based on principles that have already been adopted, as in some cases judges are not bound by decisions of other judges sitting in the same court. Precedents that have been established by higher courts should be binding on lower courts. After hearing from all sides and deciding on the facts of the case, the judge issues the appropriate decision based on the finding of fact. At present, most Common Law principles have been incorporated into statutes in most countries with some modifications. However, some legal decisions are still unwritten, for example when one needs to look at the case law and make commentaries on a specific topic. Such a legal system is different in application from one country to another. Case law in these countries is the most important source of legislation. The principles of Common Law are applied as a basic in some States without reference to statute.

One cannot imagine the application of this mechanism in arbitration, but the arbitrator might make his award in accordance with judicial precedent or consider the relevant statutes. This process also faces some challenges,³ through determining the interest legality and the law on which it is based, the grounds for refusal of enforcement, the grounds for set aside, the mandatory rules,⁴ and the law of the agreement in Common Law countries.⁵ Although the Common Law is flexible, this flexibility does not fit in with the nature of arbitration where the parties or the arbitrators cannot rely on clear rules or when the rules are not accessible to foreign lawyers. The leading countries in this system are England and the U.S. with the exception of some states such as Louisiana, which like France follows Civil Law, and those that use a mixture. In a country such

¹ Ruben Alvarado, *Common Law & Natural Rights* (Wordbridge Publishing 2009) 51.

² Akinci Law Office, 'Arbitration Processes In Common Law Vs. Civil Law Jurisdictions' [2013] *Corporate Disputes* <<http://www.corporatedisputesmagazine.com/arbitration-processes-in-common-law-vs-civil-law-jurisdictions/>>.

³ Wesley A Sturges, 'Common-Law and Statutory Arbitration: Problems Arising from Their Coexistence' (1962) 46 *Minnesota Law Review* 819 <http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=4303&context=fss_papers> Despite the fact that the reference is old, some of the facts in this Article are still pertinent.

⁴ Thomas E Carbonneau, 'Revolution in Law through Arbitration. The Eighty- Fourth Cleveland-Marshall Fund Visiting Scholar Lecture' (2008) 56 *Cleveland State Law Review* 233 <<http://engagedscholarship.csuohio.edu/cgi/viewcontent.cgi?article=1142&context=clevstlrev>>.

⁵ See *Sul América Cia Nacional de Seguros SA and Anr v Enesa Engenharia SA and Ors - EWHC (Comm)*(2012) [42].

as the U.S. which has a mix of Common and Civil Law and a mix of Common Law and written statutes, especially for usury or interest statutes, the confusion of this mix causes conflicts between states of the U.S., and between U.S. and other countries (see Chapters Four and Five).

In contrast, the Civil Law is a legal system in a written form, and supported by the parliament as the main source of law. This system is based on these written laws known as codes according to their field of application, which are constantly updated. In this system the judge issues his judgement according to the facts of the case and then applies provisions related to these facts from the law. Germany and France are the leaders of the European countries in Civil Law, and the laws of many countries are based on theirs, though some of them non-European. The Civil Law is one of the most consistent systems for arbitration in terms of clarity, but inflexibility and the needs for constant updates may also influence the choice of the parties.

The other legal system is the Islamic system, which is a mix of the Civil and the Common Law approaches and methodologies. The resources of the Islamic legal system are derived from the spirit of Islamic religion “the *Quran* and *Sunna*” and other sources, and they are named also the sources of *Sharia* law. *Sharia* law is based on Islam as a religion and provides a system to regulate trade, behaviour, worship etc. In this research, *Sharia* refers to a legal system that covers commercial laws and not a religion. Under such a legal system, the main provisions have been written in the main resources “the *Quran* and *Sunna*” and sub-provisions can be derived from these resources using other resources and methods. A group of Islamic scholars interprets the provisions of the main resources by different means and methods and with the other resources; these groups are called *madhhab* or ‘schools’. Each school has a different view with respect to interest, arbitration, its nature and meaning.

Some Islamic States follow different schools regarding to civil and commercial matters, which may cause different interpretations within those countries. Some countries follow *Sharia* law as the main source of their constitution, including Saudi Arabia, where it is considered a national law. Saudi legislation may be variously enacted by means of Royal Decrees, Royal Orders, Council of Ministers Resolutions, Ministerial Resolutions, and Ministerial Circulars. All Saudi laws are ultimately subject to and shall not contradict the *Sharia*. Saudi Arabia has commercial law, but Saudi courts and *Sharia* law do not distinguish between civil and commercial matters, which are subject to the same legal action. Other Islamic countries consider *Sharia* law as one of the main sources of their constitutions, including Egypt and the United Arab Emirates (UAE). Although these countries follow different schools, they mix *Sharia* and positive law. Egypt follows the Napoleonic code after French colonialism, and since UAE follows some aspects of Egyptian law they transitively follow the Napoleonic codes as well. These states have their

own laws in relation to arbitration and they are also signatory parties of the NYC 1958, which relates to the enforcement of foreign arbitral awards.

1.1.2 The complexity of the concepts and the issues arising from usury and interest

The definition and the concept of interest are changeable and rubbery, differing from one country to another and from one language to another. The definition of interest includes attention, advantage, attraction, benefit, hobby and stake. With regards to commerce or trade, the meaning of interest may refer to compensation and benefit, but in Arabic it refers only to profit (gain and margin). It is different in the financial industry and loan contracts, for example when a maximum interest law is violated, where it may be related to the concept of usury. Interest is a charge above what is due for a loan contract; usually this charge is a percentage of the initial amount, which is called the interest rate. This payment is for the use of credit or money and such a charge is over a period of time called the interest period. Charging excessive interest rates or more than the legal interest rate is called usury. The debate with respect to whether the meaning exclusively refers to any money above the original sum is discussed in a later section. Some of the arguments are based on morality and justice related to religious roots, while others are based on economic interests and sociological concepts. Interest can be either simple or compound. Simple interest is based on the principal amount of the loan, while compound interest is based on the principal in addition to the accumulated interest.

The influences of some financial systems such as capitalism⁶ and the diversity of cultures effects the interpretation of usury or interest. Consequently, conflicts have arisen between laws and economics, especially between the rules of justice and economic interests with regards to the interpretation of interest and usury. Interest has become a particularly difficult area in commercial law, especially with regards to international practices due to its interpretation and the impacts of these influences on it. Historically, major religions like Judaism, Christianity, and Islam⁷ prohibited usury or any interest rate on a loan, though modern legal systems often circumvent the prohibition. In *Sharia* law this concept is called *Riba* and a more detailed discussion is provided in a later section. *Sharia* law expressly prohibits *Riba*, which reflects the meaning of usury. Laws

⁶ See e.g. Edmund Clingan, *Capitalism: A Modern Economic History* (iUniverse 2015).

⁷ See Samir Abid Shaikh, *The Anatomy of Usury: A Critique of the Interest Based Economic System* (CreateSpace Independent Publishing Platform 2013) 53; 'Usury' a Universal Sin' <<http://www.giveshare.org/BibleStudy/050.usury.html>> accessed 18 August 2015; Arthur Eli Monroe, *Early Economic Thought: Selected Writings from Aristotle to Hume* (Dover Publications 2014); Constant J Mews and Ibrahim Abraham, 'Usury and Just Compensation: Religious and Financial Ethics in Historical Perspective' (2007) 72 *Journal of Business Ethics* 1 <<http://www.jstor.org/stable/25075354>>; see also Walter A Shumaker, George Foster Longsdorf and James Christopher Cahill, *The Cyclopedic Dictionary of Law* (2nd edn, The Lawbook Exchange, Ltd 2001).

in many countries stipulate that the interest rate shall not override a statutory maximum called the legal rate of the interest or usury limit.

Many countries' laws require that the interest should be a simple and not compound, and some such as England allow for whether the interest is compound or simple. Each country has its own usury law except Saudi Arabia, where interest is interpreted under *Sharia* law. In England there is no written usury code and the law is applied according to the specific case under its interpretation or precedents according to the Common Law. The interpretation or precedents depend on the main rules of the legal system, whose rules should be taken into account. However, because the Consumer Credit Act and the Unfair Terms in Consumer Contracts Regulations can be used as a law of usury,⁸ the interest rate of the Bank of England may be applied. The interest is not capped, and it is not necessary that unfair terms include an interest ceiling. England expressly refers to interest in its Arbitration Act 1996 s.49 in order to avoid misinterpretation in some respects. In Saudi Arabia, the law of *Riba* is confusing between the theoretical and practical. In U.S., there is no Federal usury statute, but each state has its own regarding interest rates and usury limits where such variation on these laws are still in effect. In most countries where the legal interest rate is exceeded or violation the usury law is legally unenforceable, under some laws usury or a charge above the legal interest rate is criminal offence and legally the entire loan contract could be declared invalid.

Interest-based loans, late payments or debt are in a different category than interest-based breaches of contract or damages, whether in the interpretation or in practice under some jurisdictions, but they are connected to each other. If a debtor would fail in paying the loan and the related interest, one of the parties may breach such a contract or the creditor may impose some damages to compensate for lost profit as a result of late payment. Thus, legal action and interest could add to the original sum plus the legal interest above the loan contract. This may be considered usury under some circumstances.⁹ It is different whether or not the late payment, breach of contract, and damages are related to credit caused by loan, mortgage, lease, or cards contracts. Some countries consider interest-based breaches of contract or actual damages to be compensation, either pre- or post-judgement, while interest with regards to loan, debt or late payment is usury. Interest with regards to late payment in the sale of contract goods or services may be compensation, though it may be considered by some to be usury. Such matters vary from one country to another depending on whether a certain matter is a substantive or a procedural matter under the law.

⁸ See Sarah Brown, 'Using the Law as a Usury Law: Definitions of Usury and Recent Developments in the Regulation of Unfair Charges in Consumer Credit Contracts' (2011) 1 *Journal of Business Law* 91.

⁹ See e.g. Grant Nelson and others, *Real Estate Finance Law, 6th (Hornbook Series)* (West Academic 2014) 528–541.

Interest is subject to either private or public law. Interest claims with regards to loan, compensations and other contracts in this regard could be easier under the national court according to its law, whether private or public. In addition, it is also simple under domestic arbitration, where it is subject to the law of the national court with regards to substantive matters. However, difficulties arise in international commercial disputes. Some international conventions have been established to regulate such transactions at this level with regards to private international law, like the Convention of International Sale of Goods (CISG) Convention, which addresses late payments and damages. One of the main goals that international conventions seek is to unite the law through establishing uniform procedures and rules, which should be adhered to by member states in their dealings organised under those conventions. The international convention is the most important element of unification in international law to promote cooperation and interdependence between nations. In addition, different organisations and associations have been instituted under the umbrella of the United Nations (UN) under public international law, such as the World Trade Organisation (WTO).

Nevertheless, these have been not yet met the aspirations of many jurisdictions, where some countries do not want to waive their laws and principles. For example, while 83 states have signed on to the CISG, Saudi Arabia and Britain are still not parties,¹⁰ because it does not fit naturally with the domestic laws. These countries are not only subject to different primary legal systems, but they are the foundation of two very different legal systems in the world. In the case of Saudi Arabia, one of the reasons that has led their decision to not enter the CISG Convention is the matter of usury and interest under Art. 78, which is contrary to *Sharia* law. However, is not necessarily the case that this article is incompatible with *Sharia* law under the concept of *Riba*.

In arbitration, the parties have a choice of the law that governs their contract, including how interest is determined. According to the nature of arbitration, such a convention may be chosen by the parties as the applicable law even if the parties are not within the Member States of CISG. Although these conventions and organisations consider arbitration as one of the main methods in resolving disputes, there has not been enough involvement internationally to find common solutions on the issue of awarding interest. In addition, there is no international convention or treaty with regards to interest-based loans.

How to determine interest in international commercial arbitration is more complex due to several overlapping legal systems and laws. One of the main differences lies in the way that the dispute is considered, whether it is substantive or a procedural. There is no uniform law

¹⁰ See 'CISG: Table of Contracting States' <<http://www.cisg.law.pace.edu/cisg/countries/entries.html>> accessed 2 September 2015.

governing these types of disputes and under different legal systems the parties, arbitrators and lawyers are required to know the aspects of each system to avoid the unexpected.¹¹

1.1.3 *The general perceptions of the nature of arbitration*

Arbitration is different in Civil Law, Common Law systems and *Sharia* law by its nature, procedures, method of evidence presentation, references to rules and laws, and interpretations of the judiciary. The parties are free to appoint the arbitrator, a number of arbitrators or an arbitration tribunal. In addition, they are free to choose the rules or law governing their arbitrable agreement, and the seat of the arbitration. Through this process the parties refer their dispute to a third party, the arbitrator. The arbitrator reviews the case and renders a resolution according to the choice of law of the parties, the choice of substantive law, the merits of the dispute, and the choice of procedural law. The parties' choice of rules is important,¹² thereby 'when parties agree to arbitration, they opt for a system in which they are free to agree upon the persons to whom they grant the power of decision'.¹³

The award by an arbitrator is binding for both parties, but such award cannot be enforced by the arbitrator. In the event a party fails to comply, a court can enforce the award.¹⁴ The arbitrator derives his jurisdiction with respect to arbitration procedures from provisions that have been stipulated by the parties in the arbitration agreement.¹⁵ If there is no such agreement, then the arbitration tribunal is allowed to implement their own procedures as they deem appropriate.¹⁶ Controversies may arise when parties fail to choose suitable laws to govern the contract, dispute or arbitration proceedings. The nature of arbitration requires the freedom of the parties to choose the applicable law and the arbitrator is free in the application of the law it deems appropriate in the event of the failure of the parties. Some national arbitration laws may require certain laws to

¹¹ Javier H Rubinstein, 'International Commercial Arbitration: Reflections at the Crossroads of the Common Law and Civil Law Traditions Perspective' (2004) 5 *Chicago Journal of International Law* 303, 308–310.

¹² Christopher Koch, 'Standards and Procedures for Disqualifying Arbitrators' (2003) 20 *Journal of International Arbitration* 325.

¹³ Howard M Holtzmann, 'Some Reflections on the Nature of Arbitration' (1993) 6 *Leiden Journal of International Law* 274.

¹⁴ Gary B Born, 'Provisional Measures in International Arbitration', *International Arbitration: Law and Practice* (Kluwer Law International 2012) 211; Albert Jan van den Berg, 'Yearbook Commercial Arbitration' [1997] Kluwer Law International; Jean M. Wenger, 'Features - Update to International Commercial Arbitration: Locating the Resources' (*law and technology resources for legal professionals*, 2004)

<<http://www.llrx.com/features/arbitration2.htm>> accessed 10 November 2015; Abdul Hamid El-Ahdab and Jalal El-Ahdab, *Arbitration with the Arab Countries* (Kluwer Law International 2011) 16.

¹⁵ Jean Francois Poudret and others, *Comparative Law of International Arbitration* (2nd edn, Sweet & Maxwell 2007).

¹⁶ Loukas A Mistelis, *Arbitration Rules-International Institutions-3rd Edition*: (Laurence Shore, Stavros L Brekoulakis and Hans Smit eds, Juris Publishing, Inc 2010) 10; James H Carter and John Fellas, *International Commercial Arbitration in New York* (Oxford University Press 2010) 77; Paul D Friedland, *Arbitration Clauses for International Contracts - 2nd Edition*: (Juris 2007) 85.

be applied, and in the event of failure of both parties to comply the seat of arbitration law would be considered. Arbitration is neutral in its nature, unlike the nature of judiciary.¹⁷

There are fundamental differences between court and arbitration, where the parties can establish that the tribunal that will decide their dispute, in addition to the power of the parties to choose or design the procedures that govern the dispute.¹⁸ Although the autonomy of the parties includes adopting established rules, they may also write their own rules, or they may leave these to the discretion of the arbitration tribunal.¹⁹ Thus, arbitration is characterised by the freedom of choice of law governing the dispute, the freedom to choose the person who settles dispute, and the freedom to choose the place of settlement. As a result, these advantages already contribute the effect of facilitating and speeding up the process and making the arbitration truly neutral. The submission to arbitration is by 'the arbitration agreement as either a clause or a submission and as an independent agreement as regards the obligation in dispute, this begs a fundamental question about the nature of the arbitration agreement.'²⁰ Arbitration clauses relating to the underlying contract agreement may affect the acceptance of arbitration and arbitration proceedings.²¹

1.1.4 Putting the issues into the context of arbitration

The New York Convention (NYC) has contributed to addressing some of the substantive and procedural issues in arbitration, leading to enforcement of the foreign arbitral awards. However, it has also enacted some grounds for refusal and gives a greater advantage to the signatory States, especially to the country of the chosen law, the country where the award is made and the country where the award is enforced. Such grounds for refusal can be interpreted differently when there are some gaps or misinterpretations of different legal systems. Every legal system has different methodology and theories regarding arbitrability, public policy and the laws applicable to the dispute or to the arbitral agreement. Even each country under such legal systems, and each state within a federal system has its own law with respect to interest. The New York Convention (NYC) has. Such a Convention has divided the recognition and enforcement into two parts; first the recognition and enforcement the arbitration agreement and second the recognition and enforcement the foreign arbitral awards.

Under the NYC, the national court in the seat of arbitration may intervene directly in the arbitral agreement, where such agreement would be unenforceable under the non-arbitrable

¹⁷ Jean M. Wenger; Albert Jan van den Berg, 'ICCA Congress Series, 1998 Paris' in Albert Jan van den Berg (ed), *Improving the Efficiency of Arbitration Agreements and Awards: 40 Years of Application of the New York Convention* (Kluwer Law International 1999) 117.

¹⁸ Holtzmann.

¹⁹ Holtzmann.

²⁰ Berg, 'ICCA Congress Series, 1998 Paris' 118.

²¹ Berg, 'ICCA Congress Series, 1998 Paris' 127, 322-337; see e.g. *Golden Ocean Group Ltd v Humpuss Intermoda Transportasi TBK Ltd and Another (The 'Barito')* [2013] EWHC 1240 (Comm).

matters in case the matter of dispute contains illegal interest or usury. A conflict could arise between the law applicable to the arbitral agreement and the law of the arbitration seat in the determining the non-arbitrable matters. In addition, the arbitral award would be unenforceable when the dispute contains illegal interest or usury under the law of the enforcement place. Thus, three laws would give effect to the determination of the non-arbitrable. If the foreign award contains interest it may not be enforced under some jurisdictions, and the arbitration would be affected, whether direct or indirect, according to the subject matter of the dispute. Further, some matters related to the interest dispute may also non-arbitrable such as bankruptcy and punitive damages. Each country has a different interpretation with regards to the question of non-arbitrable matters and interest.

Moreover, the court in the seat of arbitration could give indirect effect to the arbitration if the arbitration agreement is invalid. It must be decided who is responsible for determining the validity of the arbitration agreement and under which law such determination would be. The validity of the arbitration agreement depends on the laws of the arbitration seat, the governing arbitration agreement and the law governing the contract. In addition, bankruptcy may affect the incapacity of the parties to comply with the arbitration under different jurisdiction. Under some jurisdictions a contract that includes interest would be considered null and void, while some jurisdictions consider a contract clause that requires usury or illegal interest to be unreasonable or unconscionable and therefore would invalidate the arbitration agreement. Under the enforcement place, most the countries recognize the principle of separately, where the invalidity of the underlying contract does not invalidate the arbitration agreement.

The scope of arbitration is one of the grounds of refusal under the NYC. If the parties did not agree on the interest rate and period, the award may be refused when the arbitrator awards interest, where the matter may be considered indirect non-arbitrability due to the scope of the arbitration agreement. A question arises if the arbitration clause defines the terms of a dispute but such an agreement or the original contract does not refer directly to the awarded interest. The award may be considered outside the scope of authority of the arbitrator, thereby to what extent the arbitrator has the ability to decide the scope and the interest' rate and period. Some national arbitral laws give the arbitrator a jurisdiction to decide the scope of arbitration, and some require that the parties must agree expressly on the arbitrability and the interest rate and period, otherwise the arbitrator has no jurisdiction. Such matters differ depending on whether the parties have chosen the law applicable to the arbitration agreement or not, and whether the merit of dispute is substantive or procedurals matter, whether the parties have expressly chosen the law governing the dispute.

The international arbitral tribunals have failed to standardize procedures and approaches, and the NYC is not able to address the applicable substantive law to the merits of dispute. Considering the potential outcomes, there would be some difficulties in handling international disputes because of the conflict of laws and misinterpretation of laws and legal systems in this regard. Determining whether a particular law on the payment of interest is substantive or procedural can be an important step in the choice of law analysis because it may govern which law the arbitrator applies to resolve the claim. In many instances the arbitrator will apply the procedural rules of the seat of the arbitration and determine the substantive rules for the merits of the dispute according to the law applicable to such dispute. The court of the chosen law may also intervene in the arbitration to ensure that the law is correctly applied on the merits of the dispute, or with the power of the arbitrators to awarded interest under the agreement under the law. Thus applying invalid law would cause to be set aside or fall beyond the arbitration scope. All of these have a negative impact on the nature of arbitration, especially if of misinterpretation by national courts.

Due to the lack of choice of law, national courts may be allowed to intervene in the law applied to the merit of dispute.²² It would be more complicated if the parties failed to choose the applicable law to the contract and dispute containing interest, therefore the determination of the applicable law is subject to several trends. Some countries apply the Rome Convention to determine the substantive law applicable to the dispute. In England this convention is applied using the closest connection test, which leads to a multitude of possible outcomes. The seat of arbitration will influence which factors, such as the law of the business or place, the laws regarding debt in the place where the agreement was made, the nationalities of the parties, and the location, are taken into consideration. Moreover, in the event of conflict of laws, questions would arise as to what extent the law of the arbitration seat, or the chosen arbitration law, would impact on the law governing the contract.

This choice can be further complicated by the conflict of laws in the arbitration seat and in the place of enforcement, which would affect the awarding of interest and enforcement of the award. In addition, when laws conflict in the absence of laws governing the contract, the law of the arbitration agreement or the arbitration seat would be the applicable law to the dispute. Furthermore, to what extent these laws affect the determination of the applicable law would affect the issuance of the award through the effect on the freedom of the parties and the authority of the arbitrator under different interest laws. As mentioned earlier, in the enforcement of foreign

²² Gary B Born, *International Commercial Arbitration* (2nd ed, Kluwer Law International 2014) 3447; Berg, 'ICCA Congress Series, 1998 Paris' 118; see e.g. *Travelers Casualty and Surety Co of Europe Ltd v Sun Life Assurance Co of Canada (UK) Ltd* [2004] EWHC 1704 (Comm); see also *Arab National Bank v El Sharif Saoud Bin Masoud Bin Haza'a El-Abdali* [2004] EWHC 2381 (Comm).

arbitral awards containing illegal interest they may be found to be non-arbitrable. In addition, such an award will be rejected based on the violation of public policy in that jurisdiction.

There is no standard definition of public policy, which may be interpreted differently by a country's court. The awarding interest may be unenforceable under the NYC when an award is in violation of public policy or contrary to substantive law in the place of agreement. Under a misinterpretation of public policy, some national courts would refuse the enforcement of either the arbitration agreement or the arbitral award on the grounds of non-arbitrable matters based on their own public policy. Such action is also applied in case any contract clause is contrary to mandatory rules, substantive law or public policy. Some jurisdictions refer to the concept of international public policy to determine public policy. In summary, public policy can be a 'double-edged sword' in international commercial arbitration – 'helpful as a tool, dangerous as a weapon'²³.

1.2 Scope and Objectives

The thesis will address disputes relating to the interest on loan contracts and late payments and examine usury laws under various jurisdictions with an emphasis on *Sharia* law. Additionally, some of the issues focus on the interpretation of laws and cases and the implications of this with respect to the enforcement of arbitral awards involving interest under different jurisdictions, giving consideration to other issues in case it is needed for an appropriate interpretation.

The general objectives of this study are to examine the obstacles of enforceability in awarding of interest in international commercial arbitration within *Sharia* law and positive laws and to find a way to establish a bridge between arbitration in England, U.S., France, Saudi Arabia, UAE and Egypt. This study aims to add to the general literature on arbitration by studying usury and interest between *Sharia* law and positive laws under the New York Convention 1958, and the arbitration laws of the countries relevant to this topic while examining the following potential sources of non-enforcement of a foreign arbitral award containing interest: (1) the modern concept of arbitration under *Sharia* law, (2) the distinction between usury and interest under *Sharia* and positive laws, (3) the distinction between substantive and procedural law, (4) the distinction between applicable law to the arbitration agreement and applicable law to contract and dispute, (5) determining the direct non-arbitrability and indirect non-arbitrability; the invalidity of the arbitration agreement and an exceed the scope of the arbitral agreement, (5) the relation between non-arbitrability and public policy, (6) a definition for a public policy, (7) identifying the place of enforcement and (8) the real grounds and justifications of refusal the awarding of interest. The study generally examines the law and practice of interest and current practices for the enforcement

²³ Loukas Mistelis, 'International Law Association-London Conference (2000) Committee on International Commercial Arbitration Keeping the Unruly Horse in Control or Public Policy as a Bar to Enforcement of (Foreign) Arbitral Awards' (2000) 2 Int'l LFD Int'l 248, 248.

of awarding of interest by identifying the challenges and then proposing a set of rules and recommendations.

1.2.1 Specific Objectives

The specific objectives of this research are to address the necessary issues to fully understand the approach in each country of enforcement. Such objectives are as follows:

- i. Explore what the interest is in positive laws and *Sharia* law within the laws and practises.
- ii. Explore what the challenges are faced in international commercial arbitration in this regard.
- iii. Explore what challenges are faced in the enforcement of the awarding of interest, especially in Saudi Arabia.
- iv. To examine the influential theories, whether negative or positive, on the enforcement of foreign arbitral awards.
- v. To examine the differences between interest and usury under Islamic countries;
- vi. To identify the concept of *Riba* under *Sharia*;
- vii. To provide a necessary understanding of the *Sharia* law as a legal system.
- viii. To identify the impact of *Sharia* law on the laws of Islamic Arab countries.

1.3 Research Question

The main research question of this thesis is what obstacles may be present in the awarding of interest and enforcement of the award between positive laws and *Sharia* law?

1.4 The reasons for selecting the topic

In the beginning, the research was about the grounds for refusal in the enforcement of awarding interest in Saudi Arabia with regards to foreign awards. During the research, similar issues were also addressed by legislations and judicial decisions of other jurisdictions where relevant on this topic. Thus, it was necessary to study the laws and practices of interest in different legal systems under different jurisdictions with give more consideration to *Sharia* law. In considering the mechanism for enforcement of the awards in international commercial arbitration, it is found that most of these disputes arise because of conflicting laws. This leads to court intervention, where obstructions on settlement of these disputes results in an accumulation interest until it can reach a significant amount in any currency. It is necessary to work to develop arbitration laws in line with these disputes by tracking these gaps and trying to treat the conflicts

in line with the nature of arbitration and supporting conventions relating to the enforcement of foreign arbitral awards, and supporting arbitration to become as an alternative to the complex judicial system, especially for international parties, in order to facilitate international trade and investment.

1.5 Research Methodology

The thesis adopts the doctrinal and the comparative legal methodologies by applying primary and secondary sources from three families of legal systems: the Common, the Civil and *Sharia* laws, and the laws in countries that rely on these systems. For the Common Law and the Civil Law, cases, codes, regulations and statutes have been examined in order to understand the applications and interpretations of matters involving interest and the NYC. For *Sharia*, both primary and secondary sources have been used such as the *Quran*, *Hadiths*, *Ijma*, *Qiyas* and *Ijtihad*, and translations have been provided of the *Quran* verses and *Hadiths*, and verification of the *Hadiths*. Additionally, traditional Islamic books and modern articles and researches have been included for the purpose of understanding Islamic jurisprudence and *Sharia* law, and in particular to understand the application of both arbitration and *Riba* under *Sharia* law by using critical analysis and interpretation of the *Sharia* law sources on this matter.

One of the purposes of applying this comparative analysis is to highlight the resemblances in internationally recognised principles relating to the enforceability of arbitral awards containing interest and safeguards for the principle of party autonomy. The study compares England, the United States, France, Saudi Arabia, Egypt and the UAE under the New York Convention 1958, through the study of the reasons for rejection of foreign arbitral awards applied to these countries. The methodology used in the research is a combination of doctrinal and legal research methods in order to allow the readers to understand the definitions of interest, *Riba* and usury, and their judicial applications, as well as examining the issues which arise in the comparative context. This approach also shows the effects of different laws under different countries with respect to interest under the NYC.

The doctrinal methodology has been used to interpret the primary concepts, laws and various interpretations that have been used to examine conflicts of laws, interpretations and analysis on the applications of the NYC. The thesis also relies on secondary sources regarding the application of NYC, such as books, articles and internet sources and some legal databases such as LexisNexis, Heinonline, Westlaw, Kluwer Arbitration. Other materials relating to law and practice have been collected from different libraries and some legal materials from different jurisdictions both in Arabic and in English. In addition, various written documents, including legislations, conventions and treaties, case law, rules and conferences, have been used. Arabic

books, reports and other sources related to Saudi Arabia, Sharia law and Arabic countries have been collected and translated.

To reflect this, the research is divided into two parts. The first is a comparative study of the three legal systems and how the countries listed above deal with arbitration, interest and some of the principles of contracts and compensation. Regarding the nature of international arbitration under *Sharia* law, the research uses both comparative and 'black letter' methodology to derive governance. For *Riba*, analytical study was carried out to examine the real definition of *Riba* under *Sharia* law. The second part discusses the NYC and its applicability to relevant countries, employing comparative, analytical and critical study approaches. The thesis attempts to analyse the applicable law to the dispute and the applicable law to the arbitration agreement under the conflicting laws rules within the framework of the NYC, where conflicting laws would have different effects on the awards of interest and their enforceability. It also examines and analyses most grounds of refusal under the NYC with regard to the interest rules in these countries. The grounds were divided into two stages of the enforcement: under the enforcement of the arbitration agreement and under the enforcement of a foreign arbitral award. The analysis focuses on the main and most important issues and theories affecting the enforcement of awards containing interest under each system or State's laws.

Furthermore, the thesis gives in-depth consideration to public policy, which is the most frequently invoked ground for refusal to recognise and enforce arbitral awards. Chapter Six analyses the concept and the relation between such a concept, interest and the law. In this chapter, public policy has been divided into three types of applications by analysing the possibilities of such applications and the effect of different interpretations on the concept. In addition, the study also covers the relation between mandatory rules, rules of justice, ethical standards and public policy with regard to interest issues.

The countries studied were selected for several reasons in order to study a range of laws under different legal systems. Each of the three legal systems, Civil Law, Common Law, and *Sharia* Law are represented at least once and all countries are signatory parties to the NYC. England was included because it is a head of Common Law while France is a leader in Civil Law. The United States, as a federal country where each state has the power to create its own laws, uses a combination of Civil and Common Law. *Sharia* Law is represented by Saudi Arabia in this research, and it can also be combined with other systems: in Egypt, it is mixed with Civil Law due to French colonial influence, and the UAE, another federal country, takes the Egyptian system and further applies *Sharia*. Although there are only three systems, each country has its own theories and laws with respect to interest and usury, making for complicated international cases.

1.5.1 Gap in the current research on awarding Riba and the academic contributions of the thesis

Most of the research that discusses *Riba* provides only a general overview without thorough analysis. Previous researchers have not compared these countries in relation to disputes including interest and the issues arising from appeals for enforcement, or the application of the NYC and enforceability. For example, Baamir mentioned the practice in commercial and banking arbitration in Saudi Arabia, but he did not focus on the enforcement or study the effect of this on other countries.²⁴ In addition, he neither studied awards containing interest in different contracts nor analysed the concept of *Riba* under *Sharia* law. Moreover, he also failed to address the grounds for refusal under the NYC and the impacts of the conflicting laws in this regard.

Kutty did address Islamic contracts and arbitration in *Sharia* law, but did not address the current nature of arbitration under *Sharia*, nor provide a thorough study of *Riba* where it was related to the enforcement of foreign arbitral awards; this was typical of most research and studies.²⁵ Neither Baamir nor Kutty addresses the issue of arbitration in *Sharia* law under the international concept and modern practices, with reference to the applicable law, court intervention and enforceability. There was no specialist research in this aspect with a detailed study discussing the impact of these conflicts on enforcement. During the period of this research, some articles and books were published on the topic of usury and these have been considered in this thesis.

1.6 Overview of Thesis

The thesis includes five chapters with accompanying introduction and conclusion. Chapter two discusses international arbitration and arbitration under *Sharia* law in order to define the application of international arbitration and the nature of international arbitration under *Sharia* law. Chapter three outlines applicable laws to arbitration agreements and contracts in order to determine the validity of an arbitration agreement and the legality of interest rates, discussed further in chapter Five. Chapter four defines interest and usury as well as relevant laws and practices regarding the two in the countries of interest for this research. In addition, discusses the principles of contracts, including the autonomy of parties, good faith, and the freedom of parties with respect to contract terms and establishing contracts. It also provides a comparative study on late payment regulations in the various countries. Chapter five considers the applicability of interest and non-arbitrable matters under the seat of arbitration, the validity of arbitration agreements and underlying contracts, the scope of arbitration, and non-arbitrable matters under

²⁴ Abdulrahman Yahya Baamir, *Shari'a Law in Commercial and Banking Arbitration: Law and Practice in Saudi Arabia* (Ashgate Publishing Limited 2010).

²⁵ Faisal Kutty, 'The Shari'a Factor in International Commercial Arbitration' (2006) 28 *Loyola of Los Angeles International and Comparative Law Review* 565.

the enforcement place. Chapter Six addresses public policy as one of the grounds of refusal; this is the consequence of different interpretations of the concept of public policy which can affect the course of the arbitration process would be affected. Conflicting public policy interpretations may create disputes regarding the issue of arbitration. There are many conflicts on the concept of public policy due to the interpretation of international, domestic and transnational public policy. Substantive law and mandatory rules on public policy may also have an effect regarding interest. Also, consideration was made for the rules of justice, procedural and substantive rules regarding the rules of contract, which would affect the concept of public policy.

Chapter 2. International Arbitration and Arbitration under *Sharia* law

2.1 Introduction

Before providing an in-depth legal analysis and highlighting the scale of the problem in enforcing an award containing interest, especially in the Saudi context, it is essential to provide readers with a good understanding of how arbitration is perceived under *Sharia* law. This chapter will firstly address international arbitration in general through an examination of its nature and related disputes under different legal systems, the concept of international arbitration, and arbitration before reflecting upon the same issues in the context of the *Sharia* law. Throughout this chapter we will refer to the main challenges faced by international commercial arbitration in general. In addition, we will refer to impacts of different legal systems on arbitration and enforcement of foreign arbitral awards, and highlight fears that surround arbitration by some of the signatories of the NYC and some legal systems. All points highlighted in this chapter are intended to form the basis for cross-examination in the following chapters.

2.2 International Arbitration

International commercial arbitration is ‘the resolution of disputes between parties located in different countries and, in many cases, who come from vastly different cultures’.²⁶ International arbitration is more complex than domestic arbitration due to it being related to foreign elements or a foreign country as well as to costs.²⁷ The New York Convention 1958 was instrumental this regard on the implementation of foreign arbitral awards due to the sensitivity of the subject and its importance. In addition there are model laws, such as the law of United Nations Commission on International Trade, known as UNCITRAL Model Law 1985, which has been updated repeatedly.²⁸ Both instruments provide their own definitions of ‘international’. In accordance with the NYC, arbitration is considered international in two approaches:

‘This Convention shall apply to the recognition and enforcement of arbitration awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought, and arising out of differences between persons, whether physical or legal. It shall also apply to arbitration awards not considered as domestic awards in the State where their recognition and enforcement are sought’.²⁹

²⁶ Rubinstein.

²⁷ Anebere Stephen Ogubuike, ‘Arbitration: Is It Truly A ‘Cheap’ Alternative To Litigation’ <http://www.dundee.ac.uk/cepmlp/gateway/files.php?file=cepmlp_car13_6_734047148.pdf>.

²⁸ See ‘UNCITRAL Model Law 1985’ <http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html>.

²⁹ Article 1 of the NYC 1958.

The territorial definition given in the NYC is further expanded in the Model Law, which reads:

- ‘(a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or
- (b) one of the following places is situated outside the State in which the parties have their places of business:
 - (i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;
 - (ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected; or
 - (c) the parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one country’.³⁰

A convention is often used to achieve a high degree of consistency between the laws in participating countries, which reduces the need to further examine the law of another state party.³¹ Through the convention, the signatory state is committed for providing assurances that the law is in line with the provisions of that Convention.³² The task of interpretation is delegated to domestic jurisdictions and therefore a complete degree of uniformity may not be achieved.³³

Although the Model Law seeks to unify the law of the arbitration proceedings, it does not affect it unless the parties choose the law of countries which have expressly adopted the Model Law as their own arbitration law. Furthermore, the Model Law allows adopting states to modify or display the provisions to suit its own economic, cultural and social considerations. Most countries (153 at the time of writing) are parties to the NYC, but not the Model Law, though both facilitate arbitration in the international arena and the enforcement of foreign arbitral awards.

The Model Law is the appropriate means to unite and harmonise national laws to make adjustments to the text of the model to accommodate local requirements that vary from system to system.³⁴ Supporting the greater acceptance of the Model Law, or other convention dealing with the same subject, would lead to achieving a satisfactory degree of uniformity and flexibility. Moreover, it would encourage states to reduce the number of amendments to the Model Law when inserted in its legal system.³⁵

³⁰ Article 3 and 4 of UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006.

³¹ United Nations, ‘A Guide to UNCITRAL’ (2013) 13 <<http://www.uncitral.org/pdf/english/texts/general/12-57491-Guide-to-UNCITRAL-e.pdf>>.

³² UNITED NATIONS, ‘A Guide to UNCITRAL.’

³³ UNITED NATIONS, ‘A Guide to UNCITRAL.’

³⁴ UNITED NATIONS, ‘A Guide to UNCITRAL’ p 14.

³⁵ UNITED NATIONS, ‘A Guide to UNCITRAL’ 14–15.

States have differed in their approach to the application of the Model Law and there were some laws enacted and regional conventions held in attempt to unify the arbitration laws.³⁶ Whether the dilemma is in the NYC and arbitration laws, in their interpretation, or in the laws of usury and interest, is the subject of this research. With regards to the concept of international applicability of national arbitration laws, the situation is different. Some are compatible with the Model Law, some are different but similar to it in the general meaning, and some are completely different.

2.2.1 *The concept of international*

The concept of “international” in arbitration has a broad meaning which refers to arbitration with a foreign element or where the parties have business places in different States and refer to one of those States as the place of arbitration.³⁷ In addition, they may refer to a third country, or have their places of business in the same country but refer to arbitration somewhere else.³⁸ This concept may reflect arbitration with a non-foreign element and in the same place of the parties. Such concept is different from country to country. The national arbitration laws usually handle international arbitration differently from domestic arbitration. The different interpretations given by various legal systems may impact upon the concept of “international” in relation to arbitration. Even with the same legal term different meanings may be understood. All these would lead to confusion between the arbitrators, judges or lawyers.

Although Common Law and Civil Law have the same way to deal with many issues, there also remains significant differences between these two legal systems related to legal structure in terms of classification, fundamental concepts, terminology, etc. Nevertheless, in the case of arbitration, ‘the rules and procedures that commonly apply today in international arbitration reflect a mixture of Common Law and Civil Law norms.’³⁹ In France, ‘an arbitration is international when it involves the interests of international trade’⁴⁰ regardless of the nationality of the parties, the place of the parties, the applicable law to the merits of the dispute, or the seat of arbitration. In all cases arbitration is international if it deals with economic trade and ‘the judge acting in support of the arbitration shall be the President of the Tribunal *de grande* instance of

³⁶ A Redfern, *Law and Practice of International Commercial Arbitration* (Sweet & Maxwell 2004) 70; E Biglieri and G Prati, *Encyclopedia of Public International Law* (Elsevier Science 2014) 84.

³⁷ Richard Garnett, ‘International Arbitration Law: Progress Towards Harmonisation’ (2002) 3 *Melbourne Journal of International Law*.

³⁸ *Ibid.*

³⁹ Rubinstein 303; Caslav Pejovic, ‘Caslav Pejovic, ‘Civil Law And Common Law: Two Different Paths Leading To The Same Goal’ (2001) 32 *Victoria University of Wellington Law Review* 817 <http://www.victoria.ac.nz/law/NZACL/PDFS/Vol_6_2000/Pejovic.pdf>.

⁴⁰ Article 1504 of the Code of Civil Procedure.

Paris'.⁴¹ The judge can only intervene in international arbitration unless the parties have otherwise stipulated.⁴²

In the U.S., The Federal Arbitration Act (FAA) was updated to become consistent with the NYC and the Panama Convention, and contains three chapters: general provisions, enforcement of the NYC, and enforcement of the Panama Convention.⁴³ The FAA is considered to be federal law. The federal courts interpret its provisions and it is applied to arbitration proceedings seated in the U.S. and related to foreign commerce, where one sees “international” is defined ‘...commerce among the several states or with foreign nations’.⁴⁴ FAA section 202 makes clear that any award that involves a foreign party or foreign property, or envisages foreign performance or enforcement is non-domestic even if the arbitration takes place in the U.S. and is governed by U.S. law. Thus, Chapter two would apply, for example, to a transaction between U.S. parties that simply envisaged some foreign performance or potential enforcement against foreign assets.

In the UK the situation is different. Section 100 implements the territorial principle laid down by Art 1 of the NYC in determining the nationality of the awards, but is no definition of ‘international’ in the English Arbitration Act 1996. It refers only to an arbitration seat in England, Wales and Northern Ireland or the application of the provisions of the law if the arbitration seat has not determined.⁴⁵ There is no reference to the nationality of the parties, the place of business, or whether the dispute is of an economic nature. The 1996 Arbitration Act did not follow the Model Law, it is still subject to the general definition of the NYC with respect to the concept of international as is the case in France and the United States.

Arbitration related to two foreign states is considered international arbitration in a general sense according to the NYC. It may also be considered to be more general if there is an explicit provision in national arbitration legislation. However, it cannot neutralise the general concept of “international” in relation to disputes between two foreign signatory countries to the convention, because the explicit text of the NYC has to be taken into consideration.

Arbitration laws in the Middle East usually follow the Model Law, but the definition of “international” in these countries is wider. In Saudi arbitration law the concept is similar to the Model Law. It refers to commercial disputes, giving consideration to multiple places of business,

⁴¹ Article 1505 of the Code of Civil Procedure.

⁴² Article 1504 of the Code of Civil Procedure.

⁴³ Jeremy Wilson and William Lowery, ‘Arbitration In New York’ 1 CMS Guide to Arbitration.

⁴⁴ Carter and Fellas 5; Wilson and Lowery; Berg, ‘Yearbook Commercial Arbitration’ 1075; R Chernick, DM Kolkey and BR Neal, *Practitioner’s Handbook on International Arbitration and Mediation - Third Edition*: (Juris Net 2012) 295; Julian DM Lew, Loukas A Mistelis and Stefan Kröll, *Comparative International Commercial Arbitration* (Kluwer Law International 2003) 54.

⁴⁵ Arbitration Act 1996 ss.1, 2 and 3.

place of residence of the parties, and to an organisation or arbitration centre outside Saudi Arabia.⁴⁶ The arbitration is considered international if the dispute is related to international trade and a legal relationship around which a dispute of an economic nature revolves. It also gives effect in more than one country, regardless of the parties to the dispute.⁴⁷ Likewise in Egyptian arbitration law, but the transmittal of a permanent arbitration organisation inside or outside Egypt is considered international.⁴⁸

In UAE, there is no mention of the concept “international” in the Civil Procedure Code of the Federal Law.⁴⁹ However, after the UAE joined the New York Convention in 2006, it sought to create a new draft law on arbitration. Thus, ‘the new law will be applied to resolve commercial disputes instead of the UAE Civil Procedure Code (Federal Law No. (11) of 1992’.⁵⁰ Civil cases will be brought before the UAE civil courts, while international cases will be brought before the Abu Dhabi Federal Court of Appeal.⁵¹

The new UAE Federal Arbitration Law will be formal and make distinctions between domestic and international disputes,⁵² although the current UAE Civil Procedure Code does not.⁵³ It has been said that the arbitration law is in line with international arbitration principles, the Model Law of 1985 and its amendments in 2006.⁵⁴ However, the first ‘drafts of the law were based on the UNCITRAL Model Law, however, the latest draft is based on the Egyptian arbitration law’.⁵⁵ In general, the majority of disputes are considered in the field of international commercial arbitration.

2.3 Arbitration under *Sharia* law

Before exploring the notion of “international” and “arbitration” in 2.5 under *Sharia*, we should address the meaning of *Sharia*, the resources of *Sharia* within the Islamic legal system, Islamic schools and their impact on Islamic countries, and to what extent these countries follow *Sharia* as a resource of their constitution. We also examine the influences of Islamic schools and

⁴⁶ Art 3 of the Saudi Arbitration Law, 2012

⁴⁷ Draft Regulations for the Saudi Arbitration Law issued on July 2014.

⁴⁸ Art 3 of the Egyptian Arbitration Law 1994.

⁴⁹ Article 203 to Article 218 of the UAE Civil Procedure Code, Federal Law No. (11) of 1992.

⁵⁰ ‘Business Laws in the UAE; The New Law on Commercial Arbitration’ (*Abudhabi e-government*, 2013)

<https://www.abudhabi.ae/portal/public/en/gen_info_detail?docName=ADEGP_DF_227594_EN&_adf.ctrl-state=chxwpm4fv_4&_afLoop=4705438689059072> accessed 1 November 2015.

⁵¹ ‘Business Laws in the UAE; The New Law on Commercial Arbitration.’

⁵² Gordon Blanke and Soraya Corm-Bakhos, *The International Comparative Legal Guide: United Arab Emirates - International Arbitration 2014* (11th edn, Global Legal Group, in association with CDR, .etc 2014)

<[⁵³ Reza Mohtashami, Antonia Birt and Lee Rovinescu, ‘United Arab Emirates’ \[2013\] *International Bar Association* 3.](http://www.iclg.co.uk/practice-areas/international-arbitration-/international-arbitration-2014/united-arab-emirates>.”</p></div><div data-bbox=)

⁵⁴ ‘Business Laws in the UAE; The New Law on Commercial Arbitration.’

⁵⁵ Mohtashami, Birt and Rovinescu (n82) 20.

the Islamic legal system on usury, interest, and damages or compensation. Whether *Sharia* law is a source of legislation or not, it may have effect on the usury laws in these countries.

2.3.1 *Sharia*

There is debate about the meaning of *Sharia* and the difference between it and Islamic jurisprudence, or '*Fiqh*'. In the *Quranic* context, *Sharia* is described: 'to each of you, we prescribed a law and a method',⁵⁶ a way of life. Moreover, it is also described, 'We have established for you a code of conduct and a religion. Follow it...'⁵⁷, therefore from the Arabic meaning of the verse, it comes in the sense of a clear way, a way of religion. *Sharia* comes from the meaning of 'the pathway', approach, religion or law that should be followed.⁵⁸ *Sharia* is a religious set of laws; it also includes beliefs, acts of worship, morals, and ways of trade dealing.⁵⁹ *Sharia* does not just cover traditional rites and legal provisions; its broader concept includes all public and personal aspects of Muslim life⁶⁰ for both groups and individuals.⁶¹ The term *Sharia* has become familiar around the world,⁶² but there is misunderstanding of its meaning in some cases between Muslims and non-Muslims.

Essentially, *Sharia* means Islam as a religion, and the way or the method that leads to following this religion. Legally, it means an understanding of texts of Islam from its sources, which include texts and the analysis or the interpretation by *Qiyas* (Analogy) by using an analytical or interpretive methodology. The outcomes concluded from these sources in legal form, called "the canon" or *Sharia* law, refers to sources of Islam and the method used. It may be called Islamic *Sharia* law as a reflection of the sources and means used under Islam, and it may be called Islamic law as a reflection of a religion of Islam only. However, there is no Islamic text in a legal form, but rather through a complete methodology to extract detailed provisions.

There are those who are confuse these concepts, and Baamir believes that there is confusion between the concept of Islamic jurisprudence and *Sharia*, and that Islamic jurisprudence is variable while *Sharia* law is constant.⁶³ However, Islamic sources are constant while Islamic jurisprudence is variable depending on the circumstances; *Sharia* law also is variable according to the changing of jurisprudence and its understanding. These may be called

⁵⁶ *Quran* chap 5 verse 48 <<http://corpus.Quran.com/translation.jsp>>.

⁵⁷ 'Quran' 45 verse 18.

⁵⁸ Baamir (n 24); Mohamed Elewa Badar, *The Concept of Mens Rea in International Criminal Law: The Case for a Unified Approach* (Bloomsbury Publishing 2013).

⁵⁹ Badar; Coeli Fitzpatrick and Adam Hani Walker, *Muhammad in History, Thought, and Culture: An Encyclopedia of the Prophet of God* (ABC-CLIO 2014) 202; Baamir (n 24).

⁶⁰ One notable difference is in regard to the application of these laws, where in the *Quran* it is said *Sharia* should be applied to all human beings, but Muslim scholars believe that *Sharia* applies only to those who follow Islam.

⁶¹ See Said Ramadan, *Islamic Law, Its Scope and Equity* (Macmillan Press Ltd 1961) 62; Ahmed Afifi and Hassan Afifi, *Contemporary Interpretation of Islamic Law* (Troubador Publishing Limited 2014) xvi; Baamir (n 24).

⁶² '*Sharia*' BBC (3 September 2009) <http://www.bbc.co.uk/religion/religions/islam/beliefs/Sharia_1.shtml>.

⁶³ Baamir (n 24) .

sources of *Sharia* law, but it does not mean these sources are from *Sharia*. *Sharia* is based on these sources and the extraction of the provisions, 'the sources of legislation',⁶⁴ otherwise they may actually be called Islamic sources and *Sharia* sources. However, sources of *Sharia* law are more generally from Islamic sources, where Islamic sources fall within the scope of the sources of *Sharia* law.

Sharia law has its own methodology; it may be called the Islamic legal system, which is how to extract the provisions from detailed evidence or Islamic sources. This methodology can take place through the Islamic jurisprudence, '*Fiqh*', which leads to a judgment or a law extracted.

2.3.2 *The Structure of Islamic Law – the Islamic sources.*

2.3.2.1 Islamic jurisprudence (*Fiqh*)

Fiqh, or Islamic jurisprudence, means in Arabic a full comprehension or deep understanding.⁶⁵ A deep understanding of the Islamic sources and the extraction of Islamic provisions from these sources of study and interpretation is called *Fiqh*. *Fiqh* was established after *Sharia*,⁶⁶ but is based primarily on Islamic scholars' interpretation of *Sharia* diktats. *Fiqh* is divided and based on two branches leading to this understanding, the first one is essential and the other is secondary.

The first branch, known as *Usul al Fiqh*, is the main base for the *Fiqh* and a conductive way to understand it.⁶⁷ *Usul al Fiqh* consists of Islamic primary sources in addition to the means and methodology leading to the understanding of these sources, which are known as secondary sources. There are several definitions,⁶⁸ but it is known as a methodology that studies the sources of jurisprudence and how to reach these sources. These are *Sharia* law sources.

The second branch is '*Furu al Fiqh*' which can be translated as the branches of *Fiqh*. This branch resulted from the application of the methodology of the first branch '*Usul al Fiqh*'.⁶⁹ This part of the *Fiqh* is a written provision dealing with several classifications, including transactions and acts of worship. These provisions are based on the sources of *Sharia* law

⁶⁴ Legislation has the same meaning as *Sharia* in Arabic.

⁶⁵ Fitzpatrick and Walker 203; Baamir (n 24); M Mutaḥḥarī and H V Dastjerdi, *Noble Character of the Holy Prophet of Islam: Sira-I-Nabawi* (Alhoda Publishers & Distributors 2003) 19; CII Dodge, *The Everything Understanding Islam Book: A Complete and Easy to Read Guide to Muslim Beliefs, Practices, Traditions, and Culture* (F+W Media 2003) 104; 'Basics of Fiqh (part 1): A Brief Introduction to Fiqh' <<https://beginnerinislam.wordpress.com/2014/03/07/a-brief-introduction-to-fiqh/>> accessed 4 June 2015.

⁶⁶ Harold Motki, *The Origins of Islamic Jurisprudence: Meccan Fiqh before the Classical Schools* (1st edn, Brill Publications 2002) 4; Baamir (n 24) 1–19.

⁶⁷ Fitzpatrick and Walker 202–203; Baamir (n 24) 1–19; Mashood Baderin (ed), *Islamic Legal Theory* (Ashgate Publishing Limited 2014) <<http://eprints.soas.ac.uk/id/eprint/16852>>.

⁶⁸ See Baamir (n 24) 1–19.

⁶⁹ Fitzpatrick and Walker 203; Baamir (n 24) 1–19.

according to the rules of jurisprudence and sources of each Islamic school.⁷⁰ The first part may be considered compatible with the methodology of Common Law, while the second is compatible with the methodology of Civil Law. Thus, *Sharia* law might be considered a cross between Civil Law and Common Law.

Sources of *Sharia* law, or *Usul al Fiqh*, are constant and do not change for decades where the situation has stabilised since the rise of Islamic schools. *Furu al Fiqh* is constantly developed and decided by Islamic scholars from time to time through *Fiqh* councils and conferences. Although there are many areas of consensus, Islamic scholars sometimes differ in their opinions, depending on their method of thinking.⁷¹ For example, in regard to Islamic banking and finance, some Islamic scholars may allow certain contractual terms, while others find them unacceptable with respect to compensation for damages or interest for delays. Additionally, the same in cases for the exchange of goods or sale of goods. The same applies to contracts and the principles of contracts with regards to arbitration and its nature.

Some Islamic scholars insist on the literal wording of the *Quran* and *Hadith*, while others allow for a holistic understanding that integrates the five irrefutable sources of *Sharia* concepts. There are subsets of schools that generally interpret these five sources in differing manners. Most scholars agree on the general classification of the sources of *Sharia* law, which include primary and secondary sources. These sources were identified by Al-Shafi'i in about 800 AD⁷² and they have been agreed upon up to now. It is worth noting that the sources of *Sharia* law are hierarchical in nature, with the unchallenged *Quran* at its pinnacle.⁷³ There are two categories of *Sharia* sources; primary sources such as *Quran* and *Sunna 'Hadith'* and a variety of secondary sources. Islamic scholars have not agreed on some of those sources, but have agreed on others, such as *Ijma*, *Qiyas* and *Ijtihad*.⁷⁴

2.3.2.2 The Two Primary Sources

2.3.2.2.1 The *Quran*

The first of the primary sources of *Sharia* law is the *Quran*, which is the holy book of Islam and the direct words of God, '*Allah*', as revealed to the Prophet Muhammad.⁷⁵ The *Quran*

⁷⁰ Fitzpatrick and Walker (n 101); Baamir (n 24).

⁷¹ 'The Development of Islamic Finance in the UK: The Government's Perspective' (2008) <http://webarchive.nationalarchives.gov.uk/20130129110402/http://www.hm-treasury.gov.uk/d/islamic_finance101208.pdf> accessed 4 June 2015.

⁷² Muhammad Ibn Idris Al-Shafi'i, *Al-Risaala, Translation With An Introduction, Notes, And Appendices* (Majid Kbadduri ed, 2nd edn, 1961)

<http://d1.islamhouse.com/data/en/ih_books/single/en_Shaafi_Risaala_fi_Usul_al_Fiqh.pdf>.

⁷³ Khisz Muazzam Khan, 'Juristic Classification of Islamic Law' (1983) 6 *Houston Journal of International Law* p23-35.

⁷⁴ Afifi and Afifi xvii; Badar 30; Baamir (n 24) 1-19; Dodge 104.

⁷⁵ Afifi and Afifi p xvii; Badar 30; see also Y Dutton, *The Origins of Islamic Law: The Qur'an, the Muwatta' and Madinan Amal* (Taylor & Francis 2013).

consists of stories and news about pre-Islamic eras and about who lived in the time of the Prophet Muhammad. It also it consists of verses of provisions for many things, including worship and transactions. Those verses are known as *Quranic* texts, where a specific provision can be extracted from these texts by using the remaining sources. Other sources are applicable only when the *Quran* has little to say on a subject.

2.3.2.2.2 *Sunna (or Hadith)*

Hadith is one of the primary sources of *Sharia* law and an important source after the *Quran*. *Sunna* or *Hadith* are the sayings and practices of the Prophet Muhammad, entailing those spoken, agreed to, and acted upon.⁷⁶ Additionally, it involves rulings or judgments passed by the Prophet Mohammed on various matters. In essence, this is a collection of cases concerning personal conduct, political matters, trade, community, family relations etc., which were decided by the Prophet Mohammed and subsequently recorded. In practice, *Sunna* is used to explain that which is stated in the *Quran*, giving more provisions.

Islamic scholars in the first centuries of Islam took into account the *Hadith* when they classified sciences which serve this area and contribute to maintaining it.⁷⁷ These classifications and sciences, known as the science of *Hadith*, lay down rules distinguishing between valid, acceptable, and invalid *Hadith*.⁷⁸ Islamic scholars only rely on the provisions of the valid and acceptable *Hadith*, especially the provisions relating to transactions and acts of worship. Thus, the provisions of the *Quran* and the valid provisions of *Sunna* are considered as fundamental and main sources of legislation in *Sharia* law.

2.3.2.3 The Three Secondary Sources

2.3.2.3.1 *Qiyas (Analogy)*

Qiyas is a legal judgement created by Islamic scholars, widely regarded as the source of continuity of the *Fiqh* and based on the *Quran* and *Sunna*.⁷⁹ *Qiyas* is not a matter, but rather a method of analogical thinking based on the *Quran* and *Sunna*. Thus, *Qiyas* is the extension of *Sharia* law, provision from a known injunction, an original case to a new injunction, or a new case not found in the primary sources.⁸⁰ Fundamentally, this method is used when a scholar or judge needs a legal ruling on a new case (*fa'ra*) that is not directly shown in the *Quran* and *Sunna*.

⁷⁶ Affi and Affi xviii; Badar; see also Jonathan AC Brown, *Hadith: Oxford Bibliographies Online Research Guide* (Oxford University Press, USA 2010) 3–6.

⁷⁷ Dutton 170–180; Brown, *Hadith: Oxford Bibliographies Online Research Guide*.

⁷⁸ Suhaib Hasan, *Science of Hadith (An Introduction)* (1st edn, Dar-us-Salam 1999); see also 'An Introduction To The Science Of The Hadith' <https://archive.org/stream/AnIntroductionToTheScienceOfTheHadith-KitabMarifatAnwallm/AnIntroductionToTheScienceOfTheHadith-KitabMarifatAnwallmAl-hadithByIbnAl-salahAl-shahrazuri_djvu.txt> accessed 5 June 2015.

⁷⁹ Dodge 282; Badar; Baamir (n 24).

⁸⁰ Baamir (n 24); Badar; AK Aldohni, *The Legal and Regulatory Aspects of Islamic Banking: A Comparative Look at the United Kingdom and Malaysia* (Taylor & Francis 2012).

He may use an analogy, deduction, or legal precedent (*a'sl*) to determine the new law, sharing the same operative or effective cause '*il'lah*'.⁸¹

An example for *Qiyas* would be the prohibition of drugs in the *Quran* which provide similar effects to alcohol intoxication, which paved the way for the ban on alcohol in the Islamic world, even though there is no mention of drugs in *Sharia*.⁸² The *Quran* and *Sunna* have prohibited usury (*'Riba'*), but recent transactions and the modern style of trade did not exist in the pre-Islamic era, therefore Islamic scholars use the analogy of *Qiyas* to extract the appropriate provisions. The *Qiyas* method has been shared with the Common Law of judicial precedence in the same legal system.⁸³ However, the *Qiyas* source can only be applied by using *Ijtihad*.

2.3.2.3.2 *Ijtihad*

Ijtihad means human activity and independent judgment that leads to the formulation or discovery of a new legal provision from the sources of *Sharia* law by Scholars through applying *Qiyas* and explaining *Sharia* texts.⁸⁴ Thus, '*Ijtihad* mainly describe the mechanism of reasoning that is used to reach a decision in a case in which the main two primary resources did not provide a specific rule'⁸⁵. According to Iqbal, *Ijtihad* is referred to as 'the principle of movement in the structure of Islam.'⁸⁶ As a result, it is essential to extract the Islamic ruling or law of the main sources, which may be called a *fatwa*, or legal opinion. This legal opinion is bound to be discussed directly with evidence from the *Quran* and *Sunna* by highly-qualified Islamic scholars.⁸⁷

Ijtihad and *Qiyas* are the middle ground between the original case and the new one, using *Usul al Fiqh* and *Furu al Fiqh* in order to develop a rule or a law independently taking account of the *maqasid al Sharia* (the higher objectives or purposes of the *Sharia*).⁸⁸ To use these techniques, it is imperative that jurists have a wide knowledge of the purposes of the law so that, when choices are to be made, they will be able to choose interpretations that correspond with the spirit of the law.⁸⁹ In practice, the *Sharia* permits legal rules to be changed and modified in accordance with changing conditions.⁹⁰ The principle of *Ijtihad* is usable by those who have the

⁸¹ Aldohni 52; Ahmad Nizam Abbas, 'The Islamic Legal System In Singapore' (2010) 21 Pacific Rim Law & Policy Journal 164; John Makdisi, 'Legal Logic and Equity in Islamic Law' 33 The American Journal of Comparative Law pp 63–78.

⁸² Badar; Makdisi 63–78.

⁸³ Aldohni; Khan 47.

⁸⁴ Baamir (n 24) 1–19.

⁸⁵ Aldohni 43.

⁸⁶ Kutty (n 25) 587; Muhammad Iqbal, *The Reconstruction of Religious Thought in Islam* (Kitab Publishing House 1974) 148.

⁸⁷ Dodge 104.

⁸⁸ Kutty (n 25) 586; see also Eziuddin Mustafa Elmahjub, 'Protection Of Intellectual Property In Islamic Shari'a And The Development Of The Libyan Intellectual Property System' (Queensland University of Technology 2014).

⁸⁹ Kutty (n 25) 586.

⁹⁰ Kutty (n 25) 587.

appropriate competence. However, this principle may not fit in the agreed matters, which may be considered under the following source, '*Ijma*'.

2.3.2.3.3 *Ijma*

Al Ijma is an Arabic word which refers to consensus by collective reasoning by qualified scholars in clarifying an issue in *Fiqh* regarding issues that are not covered by the *Quran* and *Hadith*.⁹¹ Once an agreement has been established, it becomes a binding authority and cannot be repealed by another consensus.⁹² Therefore, the consensus has the effect of creating a permanent, substantive law.⁹³

Matters of worship may differ from the transaction matters and ways of notation in the branches of *Fiqh* due to the fact that they are relatively stable and clear, though there is still controversy in some transaction issues and the consensus resulting from them. The methodology of *Ijma* is stipulated in the *Quran* in the following verse: 'O you, who have believed, obey *Allah* and obey his messenger and those in authority among you. And, if you disagree over anything, refer it to *Allah* and the messenger.'⁹⁴ This referred to followers of scholars 'to the public' where the scholars' sayings come in the foreground after the *Quran* and *Sunna*; it does not refer to those who have the ability to *Ijtihad*.

The scholars that participate in *Ijma* should be qualified, which includes the prescribed methodology employed in the decision-making process. These qualifications are also required for each scholar participating individually.⁹⁵ Nevertheless, the practice of one scholar individually would be known *Ijtihad*, while the general consensus intercourse between numbers of scholars would be known as *Ijma*. Thus, some scholars believe *Ijma* is the most important legal system in *Sharia* law.⁹⁶ However, some scholarly groups believe that *Ijma* is binding despite the controversy in this regard.⁹⁷

Ijma not only refers to followers of the majority of scholars, those who have the ability to *Ijtihad*, but also to the unification and consensus of views on single issue. It 'is not a matter of consensus of a number of experts or jurists. Its meaning and function should be worked out in

⁹¹ See Omar Suleiman Al-Ashqar, *Tareekh Al Fiqh 'The History Of Fiqh - An Arabic Book* (3rd edn, Dar Alinvaais 1991) <http://ia802500.us.archive.org/17/items/tareekh_859/tareekh.pdf>; see Mohammad Omar Farooq, 'The Doctrine of Ijma: Is There a Consensus?' (2006) <<http://globalwebpost.com/farooqm/writings/islamic/ijma.doc>> accessed 7 June 2015; see Badar.

⁹² Ali Adnan Ibrahim, 'The Rise of Customary Businesses in International Financial Markets: An Introduction to Islamic Finance and the Challenges of International Integration' (2011) 23 *American University International Law Review* 679 <<http://digitalcommons.wcl.american.edu/cgi/viewcontent.cgi?article=1034&context=auilr>>; Badar.

⁹³ Farooq A Hassan, 'The Sources of Islamic Law' (1982) 76 *Proceedings of the Annual Meeting (American Society of International Law)* 65, 67 <<http://www.jstor.org/stable/25658109>>.

⁹⁴ *Quran* 4:59.

⁹⁵ Baamir (n 24) 48.

⁹⁶ Irshad Abdal-Haqq, 'Islamic Law: An Overview of Its Origin and Elements' (2002) 27 *The Journal of Islamic Law and Culture* 27–82; Baamir (n 24) 48.

⁹⁷ Kutty (n 25) 588; see also Ibrahim 679–680.

relation to the legislative function in concrete political systems, where it may produce a workable relationship between the ideal and the real'.⁹⁸ In practice, because of political divisions and cultural differences no successful consensus has emerged since the founding of Islam.⁹⁹ In addition, an absolute consensus cannot be reached in practice if even there is part consensus by scholars within one place or one Islamic school.¹⁰⁰

There are those who believe that *Ijma* is an important source and comes before *Qiyas*, and there are those who believe that there are only four sources without *Ijtihad*.¹⁰¹ Consensus cannot happen without *Ijtihad* and *Qiyas*, where *Qiyas* and *Ijtihad* are necessary to extract the judgment that will have had consensus on it by scholars. In addition, *Ijtihad* cannot happen in issues where there is an absolute consensus, even though it happens rarely. Therefore, each of the secondary sources can be before each other, but logically *Ijma* comes after the *Qiyas* and *Ijtihad*, which may be considered as the fifth source. *Ijtihad* and *Ijma* are using the same basic sources and methodology, but *Ijma* is collective.

Ijtihad should be accepted if it is based on the same methodology and the same sources, either by judges, scientists, lawyers or arbitrators, especially in light of the diversity of schools of jurisprudence, trends and views on trade transactions. Compared to the past, where there was not enough information or could it was properly accessible only by those who attended private councils or who saw these sources directly, and specifically before the codification of Islamic jurisprudence, at present it has become easy to search for those sources and access the provisions.¹⁰²

2.3.2.4 Disputed Sources

In general, Islamic scholars consider the previous five sources of *Fiqh* to be acceptable, while other influences on *Sharia* law such as *Istihsan*, *Istidlal* and *Istishab* are disputed by scholars. They are often based on the discretion of a ruling judge or body and they would take into account civil principles of equity, justice, fair play, and morality, and as such they are open to interpretation. Since these terms are subjective, the application differs from bias to bias, region to region and culture to culture. Scholars of different schools give some concepts a different name¹⁰³ and may give them different applications.

⁹⁸ Farooq, 'The Doctrine of *Ijma*: Is There a Consensus?'; AbdullHamid AbuSulayman, *The Islamic Theory of International Relations: New Directions for Islamic Methodology and Thought* (International Institute of Islamic Thought 1987) 85.

⁹⁹ Baamir (n 24) 48; Ibrahim 679–680.

¹⁰⁰ Baamir (n 24) 48; Ibrahim 679–680; AbuSulayman 75–76.

¹⁰¹ Badar referred just to four sources and *Ijma* comes before *Qiyas*; Baamir (n 24) 40–50 'Ijma is ranked higher than *Qiyas* in the order of *Fiqh* methodology'; Farooq, 'The Doctrine of *Ijma*: Is There a Consensus?' 'Ijma or consensus is one of the four sources of Islamic jurisprudence'; Dodge does not address *Ijtihad* as a source; See also Elmahjub 30–31.

¹⁰² For more info in the history of Islamic jurisprudence see Al-Ashqar; or Dutton; Motki.

¹⁰³ Baamir (n 24) 49–51.

Istihsan decisions are based on the personal choice of a judge to achieve justice or equity.¹⁰⁴ *Istislah* means the desire to get a good or beneficial result and avoid a harsh judgment.¹⁰⁵ *Istidlal* or *istishab* are pronouncements on public policy based on legal discretion.¹⁰⁶ These sources are used in cases where there is no evidence or the judge cannot figure out the effective cause (*Il'lah*¹⁰⁷) for the use of analogy (*Qiyas*) in the extraction of a new provision. In addition, *Sharia* law recognizes custom or trade uses as a source from which to extract a new provision.¹⁰⁸ These principles may be in line with some of the principles of Western laws, but they may vary from one Islamic school to another.

2.3.3 *Islamic schools*

Schools of jurisprudence developed after the Prophet's Covenant from two schools, Kufa and Medina, to four main Islamic schools: *Hanafi*, *Maliki* and *Shafi'i* and *Hanbali*.¹⁰⁹ Each adopted its own resources after the main sources and 'a different set of rules for reasoning, application and even different subordinate sources of law'.¹¹⁰ These schools differ in their interpretation of the *Sharia* sources and some of their methodology, resulting in a difference in some laws. Specifically, with regard to usury laws, they have differed in the nature of arbitration and the arbitrator's work, and to what extent arbitral awards are considered binding.

2.3.4 *The nature of arbitration under Sharia law*

Tahkeem in Arabic means the referral of the dispute for settlement by a third party as it refers to arbitration. The concept of arbitration in Arabic does not differentiate between whether the dispute would be considered by the arbitrator or judge, although the judge is appointed by the government, unlike an arbitrator. It has been known to give authorisation to a person, with the consent of the parties, to settle the dispute. Schools of jurisprudence differ in the definition of arbitration, but there is a link between these definitions.

According to the *Hanafi* school, arbitration is 'the process of choosing a person to settle a dispute' and the *Maliki* school defines it as 'the process of choosing a person to settle a dispute

¹⁰⁴ See Saim Kayadibi, *Istihsan: The Doctrine of Juristic Preference in Islamic Law* (Islamic Book Trust 2010) 12–13; Baamir (n 24) 50; Saim Kayadibi, *Doctrine of Istihsan (Juristic Preference) in Islamic Law* (Dizgi Ofset 2007); see also Haim Gerber, *Islamic Law and Culture, 1600-1840* (Boston 1999) 92–101.

¹⁰⁵ M Boroujerdi, *Mirror for the Muslim Prince: Islam and the Theory of Statecraft* (Syracuse University Press 2013) 16.

¹⁰⁶ Hassan 67; Rakesh Kumar Singh, *Textbook on Muslim Law* (Universal Law Publishing 2011) 41 but the author is confusing in the secondary sources; see Al-Shafi'i is considered as a main book in this aspect; Baamir (n 24) 50.

¹⁰⁷ Shahid Ashraf, *Judicial Culture in Islam* (Anmol Publications 2006) 197–199; Baamir (n 24) 50.

¹⁰⁸ Elmahjub 36; Baamir (n 24) 51; Kutty (n 25) 583–589.

¹⁰⁹ Abu-Umar Faruq Ahmad, *Theory and Practice of Modern Islamic Finance: The Case Analysis from Australia* (Universal-Publishers 2010) 72; see also Al-Ashqar 50.

¹¹⁰ Afifi and Afifi xxviii; Dodge 105; Aldohni 45; Baamir (n 24) 25–35; Elmahjub 23; Kutty (n 25) 580–582; Farooq, 'The Doctrine of Ijma: Is There a Consensus?'

between two or more other parties'.¹¹¹ *Shafi* defines arbitration as 'the process of choosing a person among the community to judge between disputants and settle their disputes'¹¹² and *Hanbali* defines arbitration as 'choosing an individual for the purpose of settling a dispute between two other parties and enforcing the judgment on them'.¹¹³

To make a distinction between arbitration and the judiciary in general concept, through arbitration the parties can determine the person who will settle the dispute unless they are silent. In addition, there is a contract between the parties regarding the dispute, in the modern practice called an arbitration agreement. Arbitration in Islamic law may be different in some concepts as a result of the perception of arbitration and the evidence related to it from the *Quran* and *Sunna* and other sources.

Islam recognizes arbitration and confirmed the pre-Islamic process of settling disputes, but with some changes.¹¹⁴ The legality of arbitration has been recognized by the sources of *Sharia*: the *Quran*, *Sunna*, *Qiyas* and *Ijma*. However, there was discussion among Islamic scholars over the nature of arbitration.¹¹⁵ This difference in the nature of arbitration and in its perception in Islam resulted in several negative outcomes, including to what extent arbitral awards are considered binding. In addition, there is confusion in the area of arbitration, applicable law or the law chosen, and arbitration concerning foreign parties. Therefore, we will review the concept of arbitration in the schools of jurisprudence with an analytical study.

2.3.5 Arbitration under the major Islamic schools

Although all sources of *Sharia* recognize arbitration, it does not receive any attention in the writings of the four Islamic schools. This might be attributed to the fact that the Islamic judiciary was sufficiently developed to give suitable solutions to all forms of problems which arose from public life at that time. Though arbitration is recognized by the Islamic schools as a substitute for the normal courts, every school insists on a certain idea concerning arbitration. This section will focus briefly on each school's view.

2.3.5.1 The Hanafi School

According to the *Hanafi* school, the parties can submit their dispute to arbitration in all matters except matters relating to crime.¹¹⁶ The scholars of this school uphold the contractual

¹¹¹ Baamir (n 24) 59.

¹¹² Baamir (n 24) 59.

¹¹³ Baamir (n 24) 59.

¹¹⁴ Arthur J Gemmell, 'Commercial Arbitration in the Islamic Middle East' (2006) 5 Santa Clara Journal of International Law 173.

¹¹⁵ Abdul Hamid El- Ahdab, *Arbitration with the Arab Countries* (Kluwer law international 1999) 16; Baamir (n 24); Kutty (n 25); Gemmell (n 114)175.

¹¹⁶ Baamir (n 24) 80.

nature of arbitration and confirm that arbitration is legally similar to conciliation and agency.¹¹⁷ They consider that an arbitrator works as an agent on behalf of the person who appointed him. The *Hanafi* school also stresses the connection between arbitration and conciliation.¹¹⁸ For this school an arbitral award is more similar to conciliation than to the judgement of court and has less force than the judgement of a court.¹¹⁹ Likewise, the provisions of *Majalla*, according to Kutty,¹²⁰ confirm that the arbitral awards have lesser force than court judgments and a judge can set aside these awards.

Under this school the disputing party is bound to abide by the award due to the contract of arbitration being considered binding on the parties like any other contract.¹²¹ The *Majalla* holds 'that arbitral decisions would still be binding between the parties just as a contract would be binding under the *Sharia*'.¹²² However, 'the award must be rendered unanimously, otherwise every arbitrator would be considered to have made his award separately, and this would be inconsistent with the will of the disputing parties to have an award decided by the arbitrators together'.¹²³

2.3.5.2 The *Shafi* School

Scholars in this school allow arbitration to proceed in all commercial matters but not criminal matters. Arbitration in the *Shafi* school is a legal practice if there is no a judge in the place where the dispute has arisen.¹²⁴ According to the *Shafi* school, the award of the arbitrators is inferior to that of judges because arbitrators under this school are liable to be revoked by the parties until the issuance of the award.¹²⁵ Therefore, it is compatible with the law of the *Majalla* unless the judge confirms the appointment of the arbitrator.¹²⁶

2.3.5.3 The *Hanbali* School

The unified view in the *Hanbali* school is that arbitration is permitted in commercial matters, and the arbitrator has the same jurisdiction as a judge.¹²⁷ According to this school, an award made by an arbitrator has the same binding nature as the judgement of a court,¹²⁸ but an

¹¹⁷ Baamir (n 24) 60–61.

¹¹⁸ Gemmell (n 114)175; Baamir (n 24).

¹¹⁹ Gemmell (n 114)175; Kutty (n 25) 598..

¹²⁰ Kutty (n 25) 598; see also Ahdab 19–21.

¹²¹ Gemmell (n 114)175.

¹²² Kutty (n 25) 598; Ahdab 21.

¹²³ Baamir (n 24) 61.

¹²⁴ Samir Saleh, *Commercial Arbitration in the Arab Middle East: A Study in Shari'a and Statute Law* (1st edn, Graham & Trotman 1984) 12.

¹²⁵ See Baamir (n 24) 61; Gemmell (n 114)175– 176; See also Kutty (n 25) 598..

¹²⁶ Under article 1847 of the *Majalla* cited in Baamir (n 24) 61.

¹²⁷ See Baamir (n 24) 75–80.

¹²⁸ Kutty (n 25) 598.

arbitral award has no value without judicial review.¹²⁹ The award made by an arbitrator ‘who should have the same qualifications as a judge’ is binding upon each of the parties who chose this arbitrator.¹³⁰

2.3.5.4 The *Maliki* School

The *Maliki* school believes that the application of arbitration is limited to commercial matters.¹³¹ This school has great trust in arbitration and accepts that one of the parties can be chosen to be the arbitrator by the other disputing party in the same dispute that he is a party to.¹³² Trust is shown by the fact that one party depends upon the conscience of the other.¹³³ In addition, they believe that the arbitrator’s award is binding unless there is ‘flagrant injustice’.¹³⁴ Unlike the other three schools, the *Maliki* school believes that arbitration cannot be revoked after the proceedings have begun.¹³⁵

2.4 The influences of *Sharia* sources and interpretations

Arbitration under each Islamic school is interpreted differently. Although they use the same main sources, they use different evidence with different interpretations. Most researchers study the Islamic practice of arbitration under the view and methodology of the Islamic schools, but not the modern practice of arbitration under *Sharia* law using its sources directly or using the same methodology as the schools. Through this methodology they reflect a negative image of arbitration in *Sharia* law. *Sharia* law is flexible and has an evolutionary nature, thus it would allow binding international arbitration.¹³⁶

Although some researchers have concluded that arbitration under *Sharia* law and the Islamic schools is unclear,¹³⁷ according to Kutty some commentators see arbitration simply as conciliation.¹³⁸ By contrast, the prevailing and common view between the four Islamic schools is that arbitration has a mandatory nature.¹³⁹ Although it is not explicit, the meaning is clear at face value. It is also supported by the general rules of *Sharia* law.

¹²⁹ Baamir (n 24) 75–80.

¹³⁰ Ahdab 19; Gemmell (n 114)176; Baamir (n 24) 61.

¹³¹ Baamir (n 24) 75–80.

¹³² Baamir (n 24) 61; Cited in Gemmell (n 114)175; see also Ahdab 19.

¹³³ Saleh 12.; Ahdab 21.

¹³⁴ Kutty (n 25) 598.

¹³⁵ Cited in Gemmell (n 114)175; cited in Baamir (n 24) 61.

¹³⁶ Kutty (n 25) 598.

¹³⁷ Ahmad Alkhamees, ‘International Arbitration and Shari’a Law: Context, Scope, and Intersections’ (2011) 28 *Journal of International Arbitration* 255, 264; Kutty (n 25).

¹³⁸ Kutty (n 25) 596, 598.

¹³⁹ Baamir (n 24) 60.

With regards to arbitration and its sources under *Sharia* law, there is a group that believes that arbitration in its nature is conciliation which cannot be binding on the parties.¹⁴⁰ The proponents of this view support their opinion by the following verse from the *Quran*:

‘If you fear a breach between them twain (the husband and his wife), appoint (two) arbitrators, one from his family and the other from hers; if they both wish for peace, Allah will cause their reconciliation. Indeed Allah is Ever All-Knower, Well Acquainted with all things’.¹⁴¹

Those favouring this opinion hold that the arbitrator’s award is not binding or final unless the parties accept it.¹⁴² Therefore, it is no more than conciliation and does not have a judicial nature.¹⁴³ However, this verse should not be used as evidence for arbitration because it does not describe the nature of arbitration. It is just a suggestion for reconciliation between spouses. Even if the language is explicit, there is a different meaning which takes into consideration the previous and following verses which give the whole meaning.

According to Baamir, the *Quranic* verses with regards to arbitration use the word *Hokm*, which means judgment or arbitral award, and the word *Hakam*, which means arbitrator.¹⁴⁴ Actually, it is one word with two different pronunciations; the first pronunciation means the judgement or the award, and the second the person who decides the issue. This person would be a judge, arbitrator, football referee, or person who provides advice between two or more parties. Its meaning depends on its place in the sentence.

The second opinion is on arbitration as a binding mechanism, and is based on other verses from the *Quran*. The first verse, according to Kutty, authorises those who make judgement to make decisions that are binding:¹⁴⁵

‘... and that when you judge between people you judge with justice..’.¹⁴⁶

Although it does not refer to the meaning as he stated or to the binding, it refers to the rule of justice and that the judgement should be relied under this rule:

‘And if you judge, judge between them with justice. Indeed, Allah loves those who act justly’.¹⁴⁷

The second verse, according to Baamir, says that the ‘applicable law under the *Quranic* provisions is the *Quran* itself and the *Sunna* of Prophet Muhammad; and then the other sources of *Sharia* as they have developed from the understanding of these two sources’,¹⁴⁸ as in the following:

¹⁴⁰ Ahdab 16; Cited in Kutty (n 25) 597; see also Baamir (n 24) 34.

¹⁴¹ *Quran* 4:35.

¹⁴² Baamir (n 24) 34; Kutty (n 25) 597.

¹⁴³ Baamir (n 24) 34; Kutty (n 25).

¹⁴⁴ Baamir (n 24) 34.

¹⁴⁵ See Kutty (n 25) 597.

¹⁴⁶ *Quran* 4:58.

¹⁴⁷ *Quran* 5:42.

¹⁴⁸ See Baamir (n 24) 34.

‘Surely We have revealed the Book to you with the truth that you may judge between people by means of that which Allah has taught you’¹⁴⁹

This verse refers to the *Quran* itself as a source of provision and as a main source that should be applied by a judge or an arbitrator,¹⁵⁰ but does not mention the nature of arbitration. However, the following verse is clearer in terms of referral to the both *Quran* and *Sunna*:

‘O you who believe! Obey Allah and obey the Messenger and those in authority from among you; then if you quarrel about anything, refer it to Allah and the Messenger’.¹⁵¹

The previous verses give the judge or arbitrator guidance on applicable law to the dispute through applying the primary sources and the rule of justice. The following verses may give effect to the choice of law of the parties or restrict the freedom of the parties:

‘...they will not [truly] believe until they make you, [O Muhammad], judge concerning that over which they dispute among themselves’¹⁵²

These verses give some rules and restrictions for arbitration, however, they do not refer to the nature of arbitration or to whether it is binding. The *Quran* and *Sunna* are silent in this regard to give scholars, judges and arbitrators the right to derive the provisions under these sources using the Islamic legal system, although Gemmell says that the *Quran*:

‘it appears, [it] provides no rules regarding arbitration; rather it seems to provide guidance and direction toward the use of arbitration’.¹⁵³

The *Quran* and *Sunna* are silent on way arbitration is to be used, while giving more consideration to the applicable law. This silence grants flexibility to *Sharia* law with regard to commercial arbitration. *Sharia* provides its own methodology for evolution and re-interpretation to meet the challenges of the modern era.¹⁵⁴ In general, *Sharia* law has recognized arbitration as an alternative system for settling disputes¹⁵⁵ and it does not prohibit arbitration as an alternative to the courts to settle disputes. There are disagreements between Islamic scholars within different Islamic schools but these disagreements inject Islamic laws with a degree of flexibility.¹⁵⁶

Islamic scholars disagree on whether the award of arbitration is binding and whether a non-qualified person can be appointed as arbitrator due to the fear of non-application of *Sharia* provisions. There is agreement on commercial issues being arbitrable, as these are the least harmful in *Sharia* law and are related to the rights of people. Thus, the common view among the

¹⁴⁹ *Quran* 4:105.

¹⁵⁰ *Quran* 2:213; 39:3.

¹⁵¹ *Quran* 4:59.

¹⁵² *Quran* 4:65; 24:48 and 24:51.

¹⁵³ Gemmell (n 114)193.

¹⁵⁴ Kutty (n 25) 620–624.

¹⁵⁵ Alkhamees (n 137) 255.

¹⁵⁶ Kutty (n 25) 620–624.

Islamic schools is that arbitration can be applicable in commercial matters, including international commercial arbitration.¹⁵⁷

2.5 Binding nature of arbitral award in *Sharia* law

Although there is disagreement on the nature of binding arbitral awards under the Islamic schools, that nature derives its provisions from the sources of *Sharia* law itself¹⁵⁸ and from the arbitration agreement, where *Sharia* recognizes the agreement between the parties and considers it to be binding. According to Gemmel:

Only a minority of *Shafi* scholars dissent from the generally accepted view that arbitration awards have the same *res judicata* effect as a judgment made by a *qadi*. Maliki and Hanbali commentators consider an arbitration award as binding and enforceable as an ordinary court judgment. Most Hanafi scholars and the *Medjella* require no affirmation of an arbitration award by a *qadi*.¹⁵⁹

Thus, the arbitral award is binding where the agreement to arbitration is revocable under *Sharia* law.¹⁶⁰ The general rules of contract law are applied to arbitration agreements under *Sharia* law.¹⁶¹ The concepts of *Qiyas*, *Ijtihad*, and *Ijma* together with contractual obligations (*Pacta sunt servanda*) 'make it possible to develop a viable and modern framework'.¹⁶² *Sharia* law does not distinguish between the nationality of the parties or their religion in terms of whether any agreement should be binding.

2.5.1 The concept of "international" under *Sharia* law

According to Al Mutawa, the concept of foreign and domestic arbitral awards under the NYC is in line with *Sharia*¹⁶³ and does not mention countries, nationality, or places of residence of the parties. Baamir observed that *Sharia* recognizes two main categories of legal subjects, which are Muslims and non-Muslims.¹⁶⁴

Sharia law complies with the NYC, but its international concept may be wider than the choice of the parties of this law and in terms of its followers. In some cases, it may be considered as part of the general principles of international or transnational law. It provides a legal system and general rules that can be applicable to States and individuals.

¹⁵⁷ Kutty (n 25).

¹⁵⁸ *Quran* 5:1.

¹⁵⁹ Gemmell (n 114)184.

¹⁶⁰ Gemmell (n 114)184.

¹⁶¹ Baamir (n 24) 77–85.

¹⁶² Kutty (n 25) 620–624.

¹⁶³ Ahmed M Almutawa and AFM Maniruzzaman, 'Problems Of Enforcement Of Foreign Arbitral Awards In The Gulf Cooperation Council States And The Prospect Of A Uniform Gcc Arbitration Law: An Empirical Study' 7 <http://eprints.port.ac.uk/16224/1/AHMED_ALMUTAWA_MANIRUZZAMAN_EMPIRICAL_STUDY_OCTOBER_2014.pdf>.

¹⁶⁴ Baamir (n 24) 77–85.

2.5.2 *Applicable law*

According to Al Khamees, the main difference between international arbitration and *Sharia* law is that *Sharia* restricts the freedom of the parties to select the governing law in the agreement.¹⁶⁵ However, this may be a misunderstanding. According to the principle of freedom of contract, parties to the contract are free to include any term or condition as long as these terms and conditions are not contrary to the mandatory principles of *Sharia* law.¹⁶⁶ Al Khamees believes that 'Muslims are obligated to apply *Sharia* law to resolve all their disputes'.¹⁶⁷ This would be more realistic in relation to the judicial system and its practice, where *Sharia* law is the law applicable to the dispute rather than to arbitration.

However, Al Khamees's view shall be qualified in responding to the current practice of arbitration. Regardless of whether the parties are Muslims or non-Muslims, arbitration allows freedom to choose the applicable law. With regard to the choice of applicable law, the parties have the right to choose from the rules and laws unless contrary to the rules of *Sharia*, though this choice would affect the outcome in the event that the enforcement takes a place in an Islamic country. The parties may choose either *Sharia* law or another law, or make no choice of law and leave it and its application to the arbitrators.

In the event that *Sharia* law is selected, the place of arbitration may intervene to refuse this choice or the place of execution may refuse to enforce awards according to *Sharia*. If the parties did not choose *Sharia*, the enforcement place may refuse enforcement of the award if it is contrary to the general rules of *Sharia* law in an Islamic country. This is in particular an acute issue in the case of potential conflicts between usury laws in different legal systems, especially in conflict with *Sharia* laws in this regard.

2.5.3 *The power of the arbitrator*

It is argued that the arbitrators, according to *Sharia* rules and sources, must apply *Sharia* law, but this may pose a conflict with the parties' choice of applicable law, especially if the choice was explicit. That could lead to a refusal to enforce an award which is contrary to *Sharia* law in an Islamic country if the enforcement takes place e.g. in Saudi Arabia, which requires compliance with the principles of *Sharia* law in the event of recognition or enforcement of arbitral awards. It may be easier in the case that no choice of applicable law was made by the parties that the arbitrator can apply the appropriate law under the Islamic seat. However, in international arbitration, the authority of the arbitrator may be limited by the law of the arbitration seat, the law

¹⁶⁵ Alkhamees (n 137) 264.

¹⁶⁶ Baamir (n 24) 77-85.

¹⁶⁷ Alkhamees (n 137) 264.

applicable to the arbitral agreement, the law of the place of enforcement according to national arbitration laws, or under the NYC. That could also lead to a conflict in the laws or refusal to enforce a law. It should be noted that *Sharia* law also supports the freedom of the parties.

2.5.4 Judicial review

Some Islamic countries have enacted laws to ensure non-recognition or non-enforcement of arbitral awards that are incompatible with *Sharia*. Islamic law systems give freedom to Islamic countries to apply the rules of *Sharia* and to enact regulations consistent with these rules. Consequently, there is no specific Islamic arbitration law, but a set of rules that are valid to them, to contract law and to the law governing the dispute. Some Islamic countries require that foreign awards should not be contrary to *Sharia* law and public policy, while others are limited to public policy.

Although the NYC gave signatory states the right to refuse enforcement of awards which are contrary to public policy, its purpose was to facilitate the implementation of foreign awards in signatory states. Although *Sharia* rules would support the articles of the NYC, usury laws would be in conflict with *Sharia* law or public policy, which may have effect on the enforcement of foreign awards.

Most legal systems and national arbitration laws may share the same effect on the applicable law, the power of the arbitrator and enforcement of foreign arbitral awards. They may differ on the issue of judicial review of foreign arbitral awards, and judicial intervention affects whether arbitral award is binding. Arbitration agreements are binding in all legal jurisdictions, but the fact is that there is conflict in the binding nature of arbitral award where it may be required to follow *Sharia* law and the award should comply with the principles of *Sharia*.

2.6 Conclusion

The notion of ‘international’ is very important to determine the application of NYC due to the wordings of Art 1. However, each country has its own definition, which may lead to different results in different jurisdictions. In general, arbitration is international when the award is made in a country other than the place of enforcement, or if the dispute contains a foreign element. The arbitration would also be considered international if the parties’ places of business were located in different countries, or were located outside either the seat of arbitration, the place of performance of part of the commercial obligations, or places closely connected to the subject matter of the dispute. Such locations would also affect the enforceability of the arbitral award. It may also be considered international where it is related to interest from international trade or foreign commerce or where it is subject to a foreign law, whether the dispute is considered by an

arbitration organisation or centre located inside or outside the country. The notion of 'international' is determined by the national arbitration law governing the arbitration agreement.

Different interpretations under different Islamic schools give different results on the meaning of arbitration and its nature. Such differences may also affect the meaning and interpretation of interest under Sharia Law. Arbitration by these schools is considered to be domestic arbitration rather than international arbitration. In fact, disputes in international arbitration are subject to the arbitration agreement and several foreign laws. The prevailing view in *Sharia* is that arbitrators should settle disputes according to the rules of *Sharia*. Thus, the mission of the arbitrator under *Sharia* law is similar to that entrusted to arbitrators elsewhere regarding the applicable law. With regard to commercial arbitration, a number of factors distinguish Islamic arbitration from its non-Islamic counterpart. The restriction of freedom of parties is merely limited to refusal of what leads to violation of *Sharia* law at the enforcement stage. Regardless of the concept of arbitration under Islamic schools and the implications of this concept on the nature of arbitration, in principle *Sharia* law does not prevent a referral to arbitration and it recognizes commercial arbitration. Thus, the arbitration agreement is binding in accordance with the rules and principles of *Sharia* law itself, as will be discussed.

Neither the NYC nor the Model Law is contrary to *Sharia* rules with regard to procedural and substantive rules, therefore Saudi Arabia has considered the Model Law with some amendments, but there are some comments on these amendments under *Sharia* law itself. Conflict arises only in the enforcement of the chosen foreign law governing the merits of dispute if that foreign arbitral award involves usury (*Riba*) or may contain interest, whether under Saudi arbitration law or *Sharia* law. The potential interactions between the law where arbitration takes place, the law of the arbitration agreement, the law governing the dispute, and the law of the country of enforcement will lead to complexities involving issues of the enforcement of the arbitration agreement, the enforcement of the law governing the dispute and the enforcement of the foreign arbitral award, which will be closely examined in this thesis.

Chapter 3. Applicable law to the arbitration agreement and the contract with regards to interest

3.1 Introduction

This chapter addresses the law applicable to the arbitration agreement and the merits of the dispute. The purpose of this chapter is to determine the law governing the validity of the arbitration agreement and to determine the law applicable to the dispute by the arbitrator or the arbitration tribunal. The arbitration agreement could be in the form of an arbitration clause or independent agreement arbitration, and the legal effect may be different in each case whether it is connected or separate, whether with regard to the law of the arbitration agreement or the law applicable to the dispute.

Ideally, the parties expressly choose the law governing the arbitration agreement as well as the law governing the dispute. In some cases, the parties may choose one of two laws, either the law of the arbitration agreement or the law governing the dispute. In the most difficult cases, the parties may choose neither the law of the arbitration agreement nor the law governing the dispute or the contract. Under these circumstances, it becomes necessary to the issue of applicable laws to facilitate the arbitration process, specifically with regard to interest disputes. The failure to determine the applicable law either to the arbitration agreement or the merits of the dispute may contribute to derailing the arbitration process. Failure to identify the law governing the arbitration agreement or the law and the rules that arbitration of the dispute is not compatible with the nature of arbitration.

This chapter will address the laws applicable to both the arbitration agreement and the merits of the dispute or the contract through studying arbitration laws under the NYC framework which is concerned with the enforcement of foreign arbitral awards on the international stage. The relevance of this chapter can be shown in aspects with regard to the substantive law governing the dispute, and the law that determines validity of the arbitration agreement. In particular, the existence of an arbitration agreement makes the dispute arbitrable, and the existence of conditions and rules will give effect to determining the scope of the arbitration and determines the authority of the arbitrator although, in some cases the law of the arbitration agreement would define such authority.

Conflicts may arise in such as determining the scope of dispute, the law governing the merit of dispute or the basic contract, and the applicable law to the arbitration agreement within the substantive and procedural law. The confusion is also evident in the matters of: failing to choose the law governing to the underlying contract, or the law governing to the arbitration

agreement; lack of freedom of parties to submit their disputes to arbitration, or to choose the procedural or substantive law; limitations on the choice of law; the validity of the arbitration agreement; the scope of the arbitrator's authority; the law of the arbitration seat relating to the arbitration process; the authority of the courts to review the outcome; and the law of the place of enforcement.

The problem remains if the parties failed to agree explicitly to the seat of arbitration, or if the arbitration agreement is connected to a contract governed by another law. In such situation, the agreement is subject to possibilities of unintended applicable law chosen by the tribunal. To exacerbate the issue, the laws of the places of arbitration and enforcement was offered a role to play by the NYC. In this case, conflict may arise between the foreign law of the seat of arbitration and the law of the arbitration agreement, or the law governing the arbitration clause relating to the main contract and the law of the seat of arbitration.

The matter may be more pronounced where the term 'applicable law' in the NYC may include the incapacity of the parties and invalidity of the agreement, whether or not the arbitration agreement is connected to or separate from the main contract. In France and the United States, a choice of law analysis has been adopted to determine the substantive law, but 'a choice-of-law agreement (particularly in the underlying contract) that invalidates the agreement to arbitrate will not necessarily be given effect if the law of another jurisdiction connected to the agreement would validate it'.¹⁶⁸ However 'the law governing the validity of the arbitration agreement may not be the same as the law governing the contract',¹⁶⁹ when the arbitration agreement is separate or the arbitration agreement is subject to institutional rules. It will apply different substantive legal rules to the arbitration clause.¹⁷⁰

The interaction between different choices of law related to different perspectives in arbitration may lead to the invalidation of the arbitration agreement. In developed countries, if there is no explicit choice, the principle of validation is applied. National courts have consistently been involved in the analysis of choice of the law where it has an impact in international arbitration agreement and apply what is appropriate.¹⁷¹ Art V (1)(a) of the NYC refers to the methods to ascertain the law governing the validity of the arbitration agreement.¹⁷² The law applicable to the arbitration agreement can be also determined by using such methods. However, the NYC does not give a clear meaning to Art V (1) (e) and it is silent with regard to the substantive law applicable to the contract, whether referring to the law applicable to arbitration

¹⁶⁸ Born (n 22) 577.

¹⁶⁹ Peter Ashford, *Handbook on International Commercial Arbitration* (JurisNet, LLC 2009) 10.

¹⁷⁰ Born (n 22) 575.

¹⁷¹ Born (n 22) 546–47.

¹⁷² Born (n 22) 3199.

agreement or to the law applicable to the contract, where the reasons for rejection of enforcement are still the same in both cases.

3.1.1 The impact of the seat of arbitration

The seat of arbitration is fundamental to defining the legal framework for international arbitrable proceedings, in particular its importance is imposed under Article V of the NYC. Although parties are able to select the seat of arbitration, arbitration clauses are frequently ‘pathological’, failing to designate the seat or failing to do so clearly.¹⁷³ The law of the arbitration seat gives effect to the law applicable to arbitration agreement in case of absence of such choice according to the legal effect of Art V (1) (a). The same effect occurs in the event of absence of a law applicable to the dispute, according to the legal effect of Art V (1)(c) of the NYC. There is confusion in the interpretation of this Art on whether applies to the applicable law to the contract or refers only to the law applicable to the arbitration agreement, and whether it refers to substantive or procedural matters. Born emphasizes that Article V (1)(c)’s reference is to procedural laws of arbitration.¹⁷⁴ In addition,

The substantive law applicable to the dispute is irrelevant and does not [cover] supervisory jurisdiction. For example, a U.S court held that the language of Article V (1) (c); refer exclusively to procedural and not substantive law, and more precisely to the regimen of scheme of arbitral procedural law under which the arbitration was conducted, and not the substantive law of the contract which was applied in the case.¹⁷⁵

However, some jurisdictions interpret the meaning of the Art to be for substantive applicable law to the contract and the law of arbitration seat (see chapter Five).

3.2 The law applicable to the arbitration agreement

The parties are entitled to a referral to arbitration with a choice of substantive and procedural rules that govern the arbitration agreement. The agreement shows the willingness of both parties to resort to arbitration, with the requirement to follow formal and substantive rules of the agreement under the basic international rules. An ‘arbitration agreement might permit either party to commence binding arbitration’,¹⁷⁶ and it is ‘like other contracts, in accordance with their terms’.¹⁷⁷ Therefore, under party autonomy, it is essential to demonstrate the will of the parties to resort to arbitration; the will of the parties cannot be known in the absence of such an agreement. The arbitration agreement can be in either an arbitration clause that is connected to the contract,

¹⁷³ Jonathan Hill, ‘Determining The Seat Of An International Arbitration: Party Autonomy And The Interpretation Of Arbitration Agreements’ (2014) 63 *International and Comparative Law Quarterly*.

¹⁷⁴ Born (n 22) 1065.

¹⁷⁵ Kronke 411; *Intern Standard Elec v Bidas Sociedad Anonima BT* - 745 F. Supp. 172 (S.D.N.Y. 1990) [178].

¹⁷⁶ Gary B Born, *International Arbitration: Cases and Materials* (Kluwer Law International 2011) 2011) 462–463.

¹⁷⁷ *Prima Paint Corp v Flood & Conklin Mfg Co BT - US* (1967) 388 395.

or a separate agreement. It allows submitting the dispute to arbitration, and the parties are free to establish the framework for their dispute.¹⁷⁸

The parties may choose a law that governs either the underlying contract or the arbitration agreement, or both. They may fail in the choice of law, and thus arbitrators may be free to apply the governing law. It is very simple for the main contract that contains an arbitration clause, in the event that there is a choice of law, that this choice of law will give effect on the validity of the arbitration agreement, the law applicable on the merits of dispute, and the scope of the authority of the arbitrator. The arbitration clause will usually refer to a dispute that could arise and that will be settled by arbitration, unlike the separate agreement which may refer to a dispute that has arisen, as a result affecting the determination the scope of the arbitration. Therefore, the law governing the arbitration agreement would be expressly or implicitly chosen by the parties and the implicit choice of law would also be by two methods: according to the law governing the whole contract, whether in a separate agreement form or in a form of arbitration clause, or according to the law of the arbitration seat. Such laws have the effect of determining the law applicable to the arbitration agreement. However, the conflict of laws rules determines the law applicable to the arbitration agreement and the issue of the dispute.

3.2.1 *The express choice of law agreement*

However, here there are three laws that may affect the arbitration agreement: the substantive law that governs the main contract; the chosen law of the arbitration agreement, and the law of the arbitration seat. The effect depends on whether the choice of law for the arbitration agreement was express or not. It also depends on the existence of the choice of law for the main contract and on whether the arbitration agreement was connected to the main contract or independent.

Some arbitration seats directly affect the law expressly applicable to the arbitration agreement. The effect of the arbitration seat on parties' choice of applicable law to the arbitration agreement is clear in *Arsanovia Ltd, Burley Holdings Ltd and Unitech Ltd v Cruz City 1 Mauritius Holdings*:

The difficulty that arises here and has arisen before is that the parties have chosen as the *lex causae* the law of one country, but by agreeing to resolve disputes through arbitrations with a seat elsewhere they have clearly indicated the choice of a different *lex fori*. In these circumstances, which law is (or, notionally, laws are) applicable to the arbitration agreement and determines the jurisdiction of a tribunal appointed under it? More specifically, here the *lex causae* of the SHA is (by the parties' express choice) the law of India whereas the seat of the arbitration is (by the parties' express choice) London and so the curial law of the arbitration

¹⁷⁸ As will address.

is English. Which of these two candidates is applicable to the arbitration agreement?¹⁷⁹

Despite the parties' choice of law being stated expressly on the arbitration agreement, which would give effect on the interpretation of the agreement, the seat of arbitration had a clear negative impact in this case on determining the validity of the arbitration agreement and the scope of the authority of the arbitrator. Such conflicts are not desirable, and more confusion would arise with regards to the most real connection if the choice of law was chosen either explicitly or implicitly. As

the court first decides whether the parties expressly or impliedly chose a law applicable to the arbitration agreement; if they did, the court gives effect to the parties' choice; and if they did not, the court identifies the system of law with which the arbitration agreement has its closest and most real connection.¹⁸⁰

Where the arbitration seat and the law applicable to the arbitration agreement interfere, Lord Mustill says:

the law of the arbitration agreement would only rarely be different from the law of the place (or seat) of the arbitration, and therefore his observation supported the view that the law of the seat of the arbitration had the closest and most real connection with the arbitration agreement.¹⁸¹

In *Sulamerica CIA Nacional de Seguros SA and Anr v Enesa Engenharia SA and Ors*,¹⁸² Cooke J held that the arbitration clause was governed by English law, thus the arbitration clause was governed by the law of the seat of arbitration where the seat of arbitration was London, despite the fact that the law governing the contract was Brazilian. In English law, the law applicable to the arbitration agreement is to be determined under the English conflict of laws rules; thereby the law applicable to an arbitration agreement is the closest connected law. It was held that the arbitration clause was separate from the other clauses of the contract, and there was a closer connection between the law of the arbitration seat and the law of the arbitration agreement than between the law of the underlying contract and such agreement. It was seen also that English law would validate the arbitration agreement rather than the law of Brazil. Regardless of determining the validity of the arbitration agreement by this law, the law applicable to the arbitration agreement also conflicts with the law of the contract with respect to awarding interest. In this case there was an explicit choice of the law governing the contract and it is logical that the arbitration clause is governed by this law, but the court applied the law of the seat instead.

The perspectives of parties' actual or presumed choice shows that in reality this is not always the case. It may be different if the parties have expressly opted for a different law for the

¹⁷⁹ [2012] EWHC 3702 (Comm)

¹⁸⁰ *Arsanovia Ltd v Cruz City 1 Mauritius Holdings BT - EWHC* (2012) 2012 3702.

¹⁸¹ *Ibid* at [10] (Lord Mustill), [12] (Lord Longmore), and [15] (Lord Neuberger).

¹⁸² [2012] EWHC 42 (Comm)

arbitration agreement. This is seen in the speech given by Lord Mustill in *Black Clawson International Ltd v Papierwerke Walzhpf-Aschaffenburg AG*, who firstly stated that:

Where the laws diverge at all, one will find in most instances that the law governing the continuous agreement [arbitration agreement] is the same as the substantive law of the contract in which it is embodied and that the law of the reference is the same as the *lex fori* ... In the ordinary way, [the proper law of the arbitration agreement] would be likely to follow the law of the substantive contract.¹⁸³

However, Lord Mustill later further pointed out the possibilities of its application of different laws:

Thus, there is the proper law which regulates the substantive rights and duties of the parties to the contract from which the dispute has arisen. Exceptionally, this may differ from the national law governing the interpretation of the agreement to submit the dispute to arbitration. Less exceptionally it may also differ from the national law which the parties have expressly or by implication selected to govern the relationship between themselves and the arbitrator in the conduct of the arbitration: the 'curial law' of the arbitration, as it is often called.¹⁸⁴

However, the NYC takes into account the law expressly applicable to the arbitration agreement, particularly if the parties have expressly agreed to the law governing the arbitration agreement. Such law determines the validity and interpretation of the arbitration agreement, and also determines the scope of the authority of the arbitrator. In addition, the law governing the arbitration agreement might determine the capacity of the parties. In particular, the arbitration agreement is independent of the underlying contract, and the law of the arbitration agreement is chosen explicitly. Thus, confusion arises with regards to the express choice of law for the arbitration agreement, especially when the parties have referred expressly to a seat of arbitration at the same time. As a result, the arbitration seat may be in conflict with the law of the arbitration agreement, where provision of some Arbitration Acts would be applied regardless of the law of the arbitration seat. For example, if the parties have chosen Saudi Arabia as the arbitration seat:

'The provisions of this Law shall apply to any arbitration... if this arbitration takes place in the Kingdom or is an international commercial arbitration taking place abroad and the parties thereof agree that the arbitration be subject to the provisions of this Law'.¹⁸⁵

Likewise, if the parties have adopted England as the seat, the mandatory provisions would be directly accepted regardless of the chosen law as stated in s4 (4) of the English Arbitration Act 1996: 'It is immaterial whether or not the law applicable to the parties' agreement is the law of England and Wales...'.¹⁸⁶ In addition, the law applicable to the arbitration agreement may also

¹⁸³ [1982] 2 Lloyd's Rep. 446

¹⁸⁴ In *The Channel Tunnel Case BT - AC* [1993] 334; see *Arsanovia Ltd v. Cruz City 1 Mauritius Holdings BT - EWHC*; see *Sulamerica Cia Nacional de Seguros SA v. Enesa Engenharia SA BT - EWCA Civ*; see also Albert Jan van den Berg, *Yearbook Commercial Arbitration 2008 - Volume XXXIII* (Kluwer Law International 2009) 775.

¹⁸⁵ Art 2 of the Saudi Arbitration Law 2012.

¹⁸⁶ See *C v D* [2007] EWHC 1541 (Comm) [24].

cause the explicit law governing the arbitration agreement to be ignored,¹⁸⁷ or validates the arbitration agreement. However, this may violate the NYC, which prioritizes the law governing the arbitration agreement if it was explicitly chosen.

The express choice of law for the arbitration agreement may extend to the arbitrator's decision, which would also affect the substantive law that will apply to the merits of the dispute if the parties have chosen Saudi arbitration law as the law governing the arbitration agreement.¹⁸⁸ Similarly, the Arbitration Act 1996 may also give effect to substantive applicable law or the rules of law to the issue of dispute. Under this law, the arbitrator may be given absolute authority to award interest, either simple or compound, if it is before the date of judgment or date of payment, unless there is an agreement.¹⁸⁹ This Act also states the arbitrators can apply the law considered applicable to the dispute and that their choice is the same as those of the parties in this regard.¹⁹⁰ However, other provisions may go beyond the matter of awarding interest, and that the awarding interest would be only based on the provisions of s48 and s49, but in all cases it may also be considered by the arbitrators as it considers applicable, which makes confusion.

3.2.2 *In absence of law of arbitration agreement*

If the parties have not agreed on an express choice of law on the arbitration agreement, their implied choice of law is applied. There is widespread controversy with respect to implicit choice in an arbitration agreement, such as in *Aquavita International SA and another v Ashapura Minecham Ltd*.¹⁹¹ The law of arbitration seat sometimes may be the implicit choice of law on the grounds of the closest connection test.¹⁹² The law of the arbitration seat may be the implicit choice of law for arbitral tribunals.¹⁹³ The closest connection may be based on the assumption of the existence of a law that governs the contract, otherwise the seat of arbitration would be dominant. The state that enforces the arbitral award should not base its law on the question of the validity of the agreement, unless at the request of a party¹⁹⁴ and if there is confusion between the issue of revocation, set aside, or on public policy. The enforcement state is only concerned with questions of arbitrability and public policy, and whether it is a state that implements the arbitral award. The

¹⁸⁷ *Arsanovia Ltd v. Cruz City 1 Mauritius Holdings BT - EWHC*.

¹⁸⁸ Art 38 (1) of the Saudi Arbitration Law. The parties can choose the substantive law of national law but should not conflict with Sharia provisions. As result, the chosen law would be completely contrary to Sharia law with regards to *Riba*.

¹⁸⁹ s49 of The Arbitration Act, 1996.

¹⁹⁰ See next section.

¹⁹¹ [2014] EWHC 2806; see also *Arsanovia Ltd v. Cruz City 1 Mauritius Holdings BT - EWHC*; *Sulamerica Cia Nacional de Seguros SA v Enesa Engenharia SA BT* - [2012] EWCA Civ 638.

¹⁹² See *FirstLink Investments Corp Ltd v GT Payment Pte Ltd and others* [2014] SGHCR 12; *Sulamerica Cia Nacional de Seguros SA v. Enesa Engenharia SA BT - EWCA Civ*.

¹⁹³ Ashford 10.

¹⁹⁴ See Albert Jan van den Berg, 'New York Convention of 1958: Refusals of Enforcement' (2007) 18 ICC International Court of Arbitration Bulletin 2.

arbitration agreement is still valid and binding and should be enforced by the courts and the arbitrators unless if it is found invalid under the applicable law.

If the parties failed to choose the law in the arbitration agreement, the English court may decide 'where the parties had not made any choice, the proper law would be the law with which the arbitration agreement has its closest and most real connection'¹⁹⁵ although Art V (1)(a) of NYC expressly refers to the law of arbitration seat in such an event. In *FirstLink Investments Corp Ltd v. GT Payment Pte Ltd and others*,¹⁹⁶ the Singapore High Court held that, in the absence of the express choice of law on the arbitration agreement, the parties refer implicitly to the law of arbitration seat and the governing law to the contract as a law governing the arbitration agreement. As part of the conflict of laws between the law of the arbitration seat and the substantive law that had been chosen by the parties, the court found 'that express substantive law of the contract would be taken as the parties' implicit choice of the proper law governing the arbitration agreement'.¹⁹⁷ In contrast, in *C v D* case,¹⁹⁸ the court held

that an arbitration agreement has a closer and more real connection with the place where the parties have chosen to arbitrate than with the governing law of the main contract..., the mere fact of an express substantive law in the main contract would not in and of itself be sufficient to displace parties' intention to have the law of the seat as the proper law of the arbitration agreement.

The court gives effect to the place of arbitration, despite the existence of the law applicable to the contract, and that may cause a difference in the issuance of an award and its enforceability.

The French party in *Schieds VZ*¹⁹⁹ protested under Article IV of the Rome Convention on the grounds that the dispute is a non-contractual obligation, since the arbitration clause did not refer to this type of dispute. He argued that the arbitration agreement was invalid because of its scope and because the subject of the dispute was non-arbitrable.²⁰⁰ However, the Court held that the arbitration clause was governed by the law of the seat of arbitration and that such a clause would also be governed by the substantive law of the country concerned. It is possible to imagine the conflict if the arbitration seat was Germany or if the law governing the contract was another foreign law, where a conflict would arise between the law of arbitration seat and law applicable to the dispute and the law governing the validity of the agreement and the law of the country of enforcement.

¹⁹⁵ *Sulamerica Cia Nacional de Seguros SA v. Enesa Engenharia SA BT* - [2012] EWCA Civ 638.

¹⁹⁶ [2014] SGIICR 12.

¹⁹⁷ *FirstLink Investments Corp Ltd v. GT Payment Pte Ltd and others* - SGIICR.

¹⁹⁸ *C v D* [2007] EWHC 1541 (Comm).

¹⁹⁹ (2014) 34 SchH 18 262

²⁰⁰ Thus, there is a confusion between the scope of the arbitration and the invalidity of the arbitration agreement or non-arbitrable.

These interpretations may lead to a conflict between the law applicable to the contract and the law of the seat of arbitration. The arbitration agreement can be governed by a law expressly chosen by the parties, however, there is a view ‘which holds that there is a strong presumption in favour of the law of the underlying contract also governing the arbitration agreement’.²⁰¹

3.2.2.1 The institutional rules

If the parties have not determined the arbitration seat and submitted the dispute to arbitration under a set of institutional rules, the arbitration institutions determine the law that governs the arbitration and dispute.²⁰² Arbitral centres and institutional rules of arbitration do not address the applicable law that would determine the validity of the arbitration agreement. One exception is found in the WIPO Arbitration Rules, Article 59(c) which adopts a validation principle providing that an arbitration agreement shall be ‘regarded as effective’ if it complies with the requirements of the law chosen by the parties or the law of the seat of arbitration. In contrast, some national trade associations adopt different approaches, promulgating standard form contracts and arbitration rules that implicitly adopt a specified national law applicable to both parties’ underlying contract and arbitration agreement. However, arbitration tribunals apply national law on the grounds that the arbitration clause has a close relationship with it.²⁰³

In *Dallah Real Estate and Tourism Holding Company v. Ministry of Religious Affairs, Government of Pakistan*,²⁰⁴ the parties had chosen the ICC rules as the law governing the arbitration agreement. Although the Supreme Court in England, ‘where the request of enforcement brought before’, believes in the doctrine of ‘the most and closest connection’, in this case the court ignored the ICC rules as the law governing the arbitration agreement and considered France ‘the arbitration seat’ governing the validity of the agreement.²⁰⁵ The court also rejected enforcement of the arbitration agreement due to the lack of a valid binding agreement between the parties, based on Art V (1)(a) of the NYC on the non-arbitrability. In this case, the arbitration agreement should have been treated as valid and the invalidity of the contract does not effect the validity of the arbitration agreement (see chapter five). The seat of arbitration determines the non-arbitrable matters, and the place of enforcement has no influence if there is an express law to the contract and an arbitration agreement.

²⁰¹ See also the Court of Appeal’s decision in *Sulamerica CIA Nacional de Seguros SA and others v Enesa Engenharia SA and others* [2012] EWCA Civ 638; Rachel Wilson, ‘Court Examines Relationship between the ‘seat’ of an Arbitration and the Place It Is to Be Held’ (OLSWANG, 2015) <<http://www.olswang.com/articles/2015/03/court-examines-relationship-between-the-seat-of-an-arbitration-and-the-place-it-is-to-be-held/>> accessed 30 September 2015.’

²⁰² Redfern 180–186.

²⁰³ Born (n 22) 545.

²⁰⁴ *Dallah Real Estate BT - UKSC* (2010) 2010 46.

²⁰⁵ *Dallah Real Estate BT - UKSC*.

In *SchiedsVZ*²⁰⁶ the ICC rules that govern arbitration were not able to address under the applicable law the validity of the arbitration agreement. Uncertainty arises when the parties have not determined the applicable law to the contract. Such disputes also increase unnecessary costs in addition to delaying a resolution of the dispute between the parties. If the parties select the rules of arbitration institutions and agree on the arbitration seat, the closest and real connection law governing the arbitration agreement would be the same as the law of the seat of arbitration if the arbitration institution indicated that clearly. The law of the seat of arbitration may determine the validity of the arbitration agreement, procedures and formalities, otherwise the law governing capacity would be the law of the main contract based on a closest and real connection. However, the express choice of law would be applied with respect to whether the arbitration agreement is connected or separate, and if incapacity has accrued before or after the agreement.

3.2.3 *The applicable law to the arbitration agreement*

If the arbitration clause determines the law that governs the arbitration agreement, then such law is the applicable law and would determine the validity and procedures of the arbitration regardless of the law of the underlying contract. If there were no such agreement, then the law of the underlying contract would be the applicable law to the arbitration agreement. In case there is no such choice of law, even in the underlying contract, then the law of the arbitration seat will give effect. This view was confirmed by Born, who states: ‘where the parties’ arbitration agreement would be invalid under the law of the seat of arbitration, there is every reason to apply the law governing the parties’ underlying contract to give effect to the arbitration clause’.²⁰⁷ The Swiss Law on Private International Law states that ‘an arbitration agreement shall be valid if it conforms either to the law chosen by the parties or to the law governing the subject matter of the dispute, in particular the law governing the main contract,’²⁰⁸ The applicable law has nothing to do with the merits of dispute, only to the agreement unless there is no choice of law for the underlying contract.

3.2.4 *The arbitration agreement is binding*

The existence of a valid arbitration agreement makes the case binding under arbitration. The arbitration agreement is valid and enforceable, and is binding save for incapacity of a party along with a few other exceptions. It shows the desire of the parties to be subject to the jurisdiction of arbitration. The arbitration agreement is still valid and binding, excluding preclusive effects that ‘exclude matters of mandatory law is enforceable, with the exclusion denied effect, or

²⁰⁶ Higher Regional Court of Munich, decision - *SchiedsVZ* (2014) 34 SchII 18 262.

²⁰⁷ See Born (n 22) 544–45, 784..

²⁰⁸ Article 178(2) of the Swiss Law on Private International Law; see also Born (n 22) 545.

whether it is entirely unenforceable'.²⁰⁹ In general, an arbitration agreement is considered binding in many jurisdictions and practices. As for the preclusive effects, they vary from one jurisdiction to another. For example, the parties can agree on arbitration as a binding resolution of jurisdiction disputes according to English courts and other UNCITRAL Model Law jurisdictions²¹⁰ and under U.S. law, 'where the parties have concluded a valid agreement to finally resolve jurisdictional disputes by arbitration'.²¹¹ *Sharia* considers an arbitration agreement as binding due to the fact that it is a valid contract and contains all the terms and conditions of other contracts.

In Saudi arbitration law, provided the agreement is consistent with *Sharia* with regard to interest and process, the arbitration agreement is binding unless it is invalid or voidable, likewise in Egypt and the UAE. Although:

there are doubts as to whether a non-exclusive agreement to arbitrate would even constitute an 'arbitration agreement' under applicable national and international legal regimes, at least where the results of the arbitrable process were not binding.²¹²

The mere mention of arbitration as a means to settle disputes is enough to rely on this agreement, even if not referred to directly in the issue of the dispute, especially if the agreement was made before the dispute has arisen. It remains an issue of conflict who is responsible for ensuring preclusive effects, and who determines whether the arbitration agreement binding or not, the arbitrator or the court. According to Born:

many national courts' interpretations of arbitration clauses will ordinarily be binding decisions on the merits, with preclusive effects'²¹³ ... 'if an arbitration tribunal considers whether there is a valid arbitration agreement, or whether a party lacked capacity, and concludes that no valid agreement or capacity existed, then the tribunal's resolution of the relevant factual and legal issues should be no less binding and no less subject to annulment than other jurisdictional determinations by an arbitration tribunal.'²¹⁴

His view is that an arbitration agreement should be audited and reviewed by national courts, but unfortunately this slows down the arbitration process and diminishes confidence in the arbitrator and therefore restarts the arbitration process at the beginning. If such review is made at the end of the arbitration proceedings the issuance of the award would be affected (see Chapter Five).

²⁰⁹ Born (n 22) 2706.

²¹⁰ Born (n 22) 3163–3393.

²¹¹ Born (n 22) 3214. See also Section 2 of the FAA 'requires courts to enforce [arbitration agreements] according to their terms'.

²¹² Born (n 22) 1393.

²¹³ Born (n 22) 1402.

²¹⁴ Born (n 22) 3212.

3.3 The law applicable to the contract and dispute

In arbitration, the contract is recognized and enforced by the arbitrator under the applicable law of the contract. Substantive law may be called the governing law, the applicable law, or the law of the contract.²¹⁵ The substantive law that has been chosen by the parties would be divided into two if not three forms: a substantive law governing the main contract, a substantive law governing the merits of dispute, and a substantive law governing the separate arbitration agreement with regard to a contract. Conflict may arise between the seat of arbitration law and the law governing the arbitration with regards to determining the law applicable to the contract and determining the substantive and procedural matters. A general rule is not possible due to the fact that the laws on interest vary from country to country: ‘in particular, these [laws] are considered as procedural in some countries and substantive in others’.²¹⁶ Giardina observes that

Although the legal approaches and solutions differ, even radically in the various legal systems, it is generally recognized that interest is due for delayed payments. There are also a few countries that forbid interest in principle, because they consider it inconsistent with their religious beliefs, but they provide alternative mechanisms in order to compensate the damaged party. Moreover, in some countries, interest is qualified as a procedural matter, while in others it is considered a substantive issue. There is still no uniformity as to the determination of interest rates, the period of time over which interest is due or the applicable rate. It may be added that the determination of the interest rate and period is generally fact-specific.²¹⁷

Confusions also in choice of law arise with regard to the determination of law governing damages and other interest related to compensations. Born observes that ‘the better approach is to treat damages as an aspect of the substantive law governing the parties’ dispute’.²¹⁸ This approach can not be applied as a resolution because ‘[t]here is a lack of unanimity concerning whether procedural or substantive law governs the questions whether an arbitral tribunal has the authority to award interest, and, if so, how it determines the period over which that interest accrues and the rate of interest.’²¹⁹

3.3.1 *The express choice of law*

The choice of the substantive law with respect to international arbitration is not covered in most international arbitration conventions.²²⁰ Thus, the parties’ choice of law is allowed unless

²¹⁵ Redfern 2.

²¹⁶ Andrea Giardina, ‘Issues of Applicable Law and Uniform Law on Interest: Basic Distinctions in National and International Practice’ in Laurent Levy and Filip de Ly (eds), *Interest, Auxiliary and Alternative Remedies in International Arbitration* (International Chamber of Commerce (ICC) 2008) 129.

²¹⁷ Giardina 141.

²¹⁸ Born (n 22) 2670.

²¹⁹ John Y Gotanda, ‘Awarding Interest in International Arbitration’ [1996] *American Journal of International Law* 40, 51.

²²⁰ Born (n 22) 2620.

it conflicts with mandatory national laws or public policies. International conventions and treaties affect the choice of substantive law in international commercial arbitration. However, most arbitration acts allow the parties to choose the substantive law of the national law.²²¹ The arbitration tribunal shall determine the outcome of a dispute regarding the parties' agreement.²²² The parties can expressly choose the substantive law that would govern their contract and dispute, or contract additionally that arbitrators and national courts shall apply the parties' choice of law unless otherwise agreed.

A conflict arises where the seat of arbitration and the law governing the arbitration agreement affect the express choice of law governing the merit of dispute, or vice versa. Where some arbitration laws affect the law applicable to merit of dispute, such as the Saudi Arbitration Law and the England Arbitration Act, as well as the influence of their arbitration seat. Nevertheless, the English Arbitration Act, for example, would be applied even outside England and would give effect to the arbitration seat anywhere.²²³ In addition, whatever the law applicable to the agreement of the parties, the English law is applied if it is contrary to the mandatory rules.²²⁴ Likewise, the Saudi Arbitration Act states that arbitration 'takes place in the Kingdom or is an international commercial arbitration taking place abroad and the parties thereof agree that the arbitration be subject to the provisions of this Law'.²²⁵ In addition, *Sharia* gives effect and indirectly applies whatever the express law in case it is contrary to *Sharia*.²²⁶ However, neither the seat of arbitration nor the law govern the arbitration agreement should give effect according to the freedom of parties (see Chapter Four).

Accordingly, the express law governing the contract should be applicable to the contract clauses and dispute, whether the contract is connected to or separate from the arbitration agreement, with no regard to the law of the arbitration agreement or the law of the arbitration seat due to the lack of effect and freedom of the parties. Therefore, in the enforcement phase of the contract and the law applicable to it, it should only consider these effects with respect to arbitration proceedings, even if such law is a set of rules which regulates and identifies the functions of the arbitrator and the arbitration tribunal. Four laws may be at play in such matter; the law of the arbitration seat, the law of the arbitration agreement, the law of the contract and the

²²¹ Art 28 (1) of UNCITRAL Model Law, see Art 4 (3) & s 46 (2) of the England Arbitration Act 1996, see Art 38 & 50 of the Saudi Arbitration Law 2012, Egyptian Arbitration Law 1994 etc. See also Ashford 10.

²²² Art 35 of UNCITRAL Arbitration Rules, see s46 (1), (4) of the England Arbitration Act 1996, see Art 38 & 50 of the Saudi Arbitration Law 2012, Egyptian Arbitration Law 1994 etc.

²²³ For example, if the parties choose the English Arbitration Act as a law governing the arbitration agreement, thus, this Act will '... apply where the seat of the arbitration is in England... [and] ... apply even if the seat of the arbitration is outside England'. See Art s2 (1) &(2) of the English Arbitration Act 1996, See also *C v D case (n 643)* [24].

²²⁴ See s4 (4) of the England Arbitration Act 1996.

²²⁵ Art 2 of Saudi Arbitration Act 2012.

²²⁶ Art 38 (1) (a) of the Saudi Arbitration Law.

law of the enforcing court. However, the law of the arbitration seat does not affect either the contract or disputes or the arbitration process if there is an explicit law for each.

3.3.2 *Without express choice of law*

The wrong determination of the law applicable to the contract may give a different result. Such result affects the enforceability of the award where two or more laws would conflict in determination of the law applicable to the contract, and that the award may be set aside under Art V (1) (e) or considered beyond the scope of arbitration according to Art V (1) (c). Two laws may be influential in determining the law governing the dispute in absence of a law applicable to the contract. The law governing the arbitration agreement and the law of the arbitration seat would give effect in determining the law applicable to the merits of dispute according to the interpretation of Art V (1) (e). It is not necessary that the parties have agreed on the seat of arbitration, where it might be that the law of the arbitration agreement has an impact, and whether it is connected to or separate from the contract whether or not the parties are agreed to the law of the arbitration agreement. However, such conflict and differences will definitely affect the enforcement of foreign arbitral awards involving interest where is considered a substantive law under the law of the place of enforcement. Thus, 'it cannot always be assumed that commercial parties want the same system of law to govern their relationship of performing the substantive obligations under the contract, and the quite separate (and often unhappy) relationship of resolving disputes'²²⁷ and 'the natural inference would instead be to the contrary'.²²⁸

Some jurisdictions apply the conflict of laws rules on the merit of dispute even if the parties agree to a choice of law. The parties may or may not choose such terms and if they fail to choose they leave the matter to consideration by the arbitrator under the applicable law. Some countries require that if there is no law governing the contract the arbitrators do not apply conflict of laws rules unless the parties agree, such as in Saudi Arabia and Egypt.²²⁹ In the theory of analysis of conflict of laws in determining the law applicable to the arbitration agreement, the rules are also used to determine the law applicable to the merits of the dispute in international commercial arbitration²³⁰ under different approaches, where it is considered applicable,²³¹

²²⁷ *FirstLink Investments Corp Ltd v. GT Payment Pte Ltd and others* [2014] SGHCR

²²⁸ *FirstLink Investments Corp Ltd v. GT Payment Pte Ltd and others* [2014] SGHCR

²²⁹ See Art 38 of the Saudi Arbitration Law; see also Art 39 of the Egyptian Arbitration Law.

²³⁰ See United Nations 14.

²³¹ See s46 (4) of English Arbitration Act. It takes the reverse legal effect in the absence of law governing the arbitration agreement, and controversy in such a matter, or indirectly from what it considers applicable. See s46 (1) (b) and s46 (3) of the Arbitration Act, 1996, 'If the parties so agree, in accordance with such other considerations as are agreed by them or determined by the tribunal... If or to the extent that there is no such choice or agreement, the tribunal shall apply the law determined by the conflict of laws rules which it considers applicable'; Similar the UNCITRAL Model Law, Art 28(2) 'Failing any designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable'; See also Art 35 (1) of the UNCITRAL Arbitration Rules; see also Slovenian Arbitration Law, Art. 32(2) 'Failing any designation by the parties, the arbitral tribunal shall apply the rules of law which it considers applicable'.

appropriate,²³² or closely connected. Most laws and jurisdictions directly follow the theory of applying as it deems appropriate if failing any indication. Arbitrators usually determine the applicable law by applying the rules of conflict of laws as they deem appropriate.²³³ Arbitral tribunals in the seats of both Common Law and Civil Law applied the substantive laws of the seat of arbitration as an implied agreement of the parties.²³⁴ However, the position in Common Law is that matters of compensation, including damages, are governed by the law of the forum, the seat of arbitration, while the position in Civil Law is generally that matters of damages and compensation were governed by statute.²³⁵ The substantive law is determined by applying the rules of conflicts of law by the arbitration tribunal.²³⁶

3.3.2.1 Conflict of laws rules

Conflict of laws rules are different across jurisdictions. The approach of many Civil and Common-law countries with respect to determining the applicable law on dispute is to apply the seat of arbitration's choice of law rules.²³⁷ However, English courts apply the implicit choice in the absence of an express law. Moreover, 'the 1998 Act or indeed to any other substantive obligations which arise as a matter of English law',²³⁸ and 'consider the application of the Unfair Contract Terms Act 1977 to a no set off clause in loan agreements between a foreign bank and foreign [party/company]'.²³⁹ In *Martrade Shipping & Transport GmbH v United Enterprises Corporation*,²⁴⁰ the Court did examine the possibility of the application of Late Payment Act 1998 and the Unfair Contract Terms Act 1977 under the closest connection test. In addition, the court tested the application of the Rome Convention²⁴¹. It found there was no sufficient connection between the contract and English law, although the arbitration clause stated that arbitration was

²³² Art 1511 of the French Code of Civil Procedure provides that the arbitral tribunal may resolve the dispute 'in accordance with the rules of law it considers appropriate'; ICC Rules, article 17.1 enable the arbitration tribunal to determine the law applicable to the substance of the conflict: 'The parties shall be free to agree upon the rules of law to be applied by the Arbitral Tribunal to the merits of the dispute. In the absence of any such agreement, the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate'; see also Other legislation, in Europe and elsewhere, is similar see, e.g., Netherlands Code of Civil Procedure, Art.1054 (2) 'in accordance with the rules of law it considers appropriate'; Indian Arbitration and Conciliation Act, Art. 28(1)(b)(iii) 'apply the rules of law it considers to be appropriate given the circumstances surrounding the dispute'; Hungarian Arbitration Act, 49(2).

²³³ Born (n 22) 2634.

²³⁴ ICC Case No. 11849 of 2003, in ICC Case No. 9771 of 2001 cited in Giardina 139–40; Born (n 22) 2639.; ICC Case No. 2735, 104 J.D.I. (Clunet) 947 (1977); ICC Case No. 2391, 104 J.D.I. (Clunet) 949 (1977); Art 187(1) of Federal Statute on Private International Law (Switz.).

²³⁵ Born (n 22) 2670; Giardina 129.

²³⁶ Ashford 8–10; G Born, *International Commercial Arbitration: International and USA Spectscmentary and Materials* (Springer Netherlands 2001) 42,526; John B Tieder, 'Factors to Consider in the Choice of Procedural and Substantive Law in International Arbitration' (2003) 20 Journal of International Arbitration 393, 400.

²³⁷ Born (n 22) 2629, 2637.

²³⁸ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm) [21].

²³⁹ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm) [26].

²⁴⁰ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm).

²⁴¹ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm) [33]'In this case the tribunal did not make reference to the Rome Convention. It may have been as a result of failing to distinguish between Article 3 (choice) and Article 4 (connecting factors) that they were led into error in treating the arbitration clause as a powerful indication in favour of English law'.

seated in London. The Court found that the the arbitration clause did not indicate that the contract is subject to the law of England, because the parties did not explicitly choose that the contract was to be governed by English law or English rules of conflict of laws as '[t]hey must provide a real connection between the contract and the effect of prompt payment of debts on the economic life of the United Kingdom'.²⁴² In England, in absence of the law applicable to the contract, consideration is given if there is an express or implicit national law and therefore applies the closest connection test. In most cases the law of the arbitration seat is applied as previously stated in (impact of the arbitration seat). In case there is no indication of an applicable national law, Art 4 of the Rome Convention can be applied to determine the applicable law to the contract.

When the Rome Convention is applied, most arbitration tribunals seated in contracting states have concluded that the Rome Convention was potentially applicable in the same manner as a national choice of law rule to determine the substantive law applicable to contractual obligations in an international arbitration.²⁴³ Rome I provides the freedom of the parties to choose the law and provides clear rules to determine the applicable law to the contract where there is an absence of choice or failure to reach agreement. It also allows choice of law governing contractual obligations in civil and commercial matters, while Rome II covers the law applicable to non-contractual obligations. The Rome Convention has different ways of determining the applicable law, which are often linked to place of occurrence of the damage.²⁴⁴ It does not apply if the contract is closely connected to the law of another state,²⁴⁵ it cannot be applied to non-contracting states, and is not in line with the NYC convention with regards to the applicable law under Art V (1).

In France and the United States, a choice of law analysis has been adopted to determine the substantive law.²⁴⁶ In France, the arbitrators shall decide the dispute according to the chosen rules of law or according to the rules of law it considers appropriate and shall trade usages into account if no choice has been made.²⁴⁷ The arbitrator is not required to apply a conflict rule of specific national law, here the arbitrators have power to use the appropriate rules but must give reasons for such decision and consider the mandatory rules.²⁴⁸ In England the arbitrators are free

²⁴² *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWTC 1884 (Comm) [17].

²⁴³ Alexander Bělohávek, *Rome Convention - Rome I Regulation*: (Juris 2011); see also Francisco J Garcimartín Alferez, 'The Rome I Regulation: Much Ado about Nothing?' [2008] The European Legal Forum <<http://www.simons-law.com/library/pdf/e/884.pdf>>.

²⁴⁴ Art 4 of Rome II; Article 14(2) and (3) of Rome II.

²⁴⁵ Art 4(5) of Rome II.

²⁴⁶ Born (n 22) 577 'In each of these jurisdictions, a choice-of-law agreement (particularly in the underlying contract) that invalidates the agreement to arbitrate will not necessarily be given effect if the law of another jurisdiction connected to the agreement would validate it.'

²⁴⁷ Art 1511 of the French CPC.

²⁴⁸ Thomas H Webster and Dr Michael Buhler, *Handbook of ICC Arbitration: Commentary, Precedents, Materials* (3rd edn, Sweet & Maxwell 2014) 299.

to determine the conflict of laws rules as it considers applicable,²⁴⁹ such decision is considered as chosen by the parties,²⁵⁰ but the public policy should take into account.²⁵¹ The power and functions of arbitrators differ between Common and Civil Law systems, especially in distinguishing between procedural and substantive matters.²⁵² However,

the arbitrators may have recourse to the conflict rules of one or more States, or to general principles of private international law. They can also resort to the direct method, which enables them to avoid using a conflicts approach and to select the appropriate rules for the purpose of resolving the dispute.²⁵³

Arbitral Tribunals seated in Saudi Arabia or other Islamic countries, or those which are subject to their arbitration laws in those countries, are limited to considering the applicable laws in accordance with *Sharia* law, public order or national non-conflict of laws rules. They must interpret the choices of the parties through a review of all the laws that govern and give effect in the arbitration, which may be difficult.²⁵⁴ Hence, in the total absence of the law governing the contract or the absence of one of the implicit considerations, the applicable law of the country where the award would be enforced and the parties' agreement or part of the contract may take more consideration.

3.3.2.2 National law

Most laws refer directly or indirectly to a national law or rules of law, and because of that every rule is subject to the legal system. The result is similar to what Mann stated:

In the legal sense, no international commercial arbitration exists. Just as, notwithstanding its notoriously misleading name, every system of private international law is a system of national law, every arbitration is a national arbitration, that is to say, subject to a specific system of national law.... every arbitration is necessarily subject to the law of a given state.... the law of the arbitration tribunal's seat initially governs the whole of the tribunal's life and work. In particular, it governs... the rules of the conflict of laws to be followed by [the arbitrators].²⁵⁵

Thus, the arbitrators have the adjudicative character in the international arbitration to settle the dispute neutrally, confidentially, quickly, and flexibly. According to different national

²⁴⁹ See s46 (4) of English Arbitration

²⁵⁰ The selection of the arbitral tribunal shall be considered as chosen by the parties in the absence of any express or implied agreement. See s4 (5) of the Arbitration Act, 1996, "or which is objectively determined in the absence of any express or implied choice, shall be treated as chosen by the parties"

²⁵¹ See e.g. *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm) [11–15].

²⁵² J Martin Hunter and others, 'Awarding Interest in International Arbitration: Some Observations Based on a Comparative Study of the Laws of England and Germany' (1989) 6 *Journal of International Arbitration* 7.

²⁵³ UNITED NATIONS, 'UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT; The Law Governing the Merits of the Dispute' 17.

²⁵⁴ UNITED NATIONS, 'UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT; The Law Governing the Merits of the Dispute' 11.

²⁵⁵ See Francis Mann, 'Lex Facit Arbitrum' in Pieter Sanders (ed), *International Commercial Arbitration* (The Hague:Martinus Nijhoff 1986) 241, 244–45, 248; see also Born (n 22) 2629.

legal systems, they can consider and determine the applicable law to the parties' dispute, the law applicable to the arbitration agreement, the arbitration proceedings in accordance with the seat of arbitration, and avoid reasons for refusal of enforcement.

The national law or the chosen law of parties, whether express or implicit, is the factor to be considered when determining the applicable law of the contract, merit of dispute, validity, and the terms of the parties. However, there is also confusion with regards to identifying the national law – for example, some countries do not consider *Sharia* law to be a national law that can be applied even when disputing parties have chosen it. In *Beximco Pharmaceuticals v. Shamil Bank of Bahrain EC*,²⁵⁶ the Court of Appeal in England, upholding the lower court's decision, stated that the law under which the case is tried should be the law of a country. *Sharia* law, according to the Court, did not meet this requirement, and was therefore unenforceable.²⁵⁷ Thus, the court refused to accept *Sharia* law as the applicable law in combination with English law. The Court of Appeal held in this case that the applicable law in an international commercial contract should be a national law according to the Rome Convention.²⁵⁸ Thus, the court considered *Sharia* law is a 'non-national law' and it did not meet with the Convention.

However, *Sharia* law is a legal system and a national law in some countries, as explained above. In addition, the parties can choose the provisos of CISG, even they are not parties to the convention, and they can choose *lex mercatoria* under the freedom of contract.²⁵⁹ The Rome Convention, however, is not applicable to non-contractual countries. The outcome of the Court's decision ignored *Sharia* law as a legal system. Despite that the fact that English law recognizes the freedom of the parties in the choice of law and the rules that govern the contract, the Court held that *Sharia* law is not a legal system.

²⁵⁶ *Beximco Pharmaceuticals v. Shamil Bank of Bahrain EC* [2004] case No A3/2003/1952, [2004] EWCA Civ 19, 2004 WL 62027. The total judgment sum awarded was some US \$49.7 million. The appellants were refused permission to appeal by Morison J, but Clarke LJ gave permission on 17 September 2003 in respect of a single issue relating to the construction and effect of the form of the governing law clause that included in the Murabaha agreements. That clause pointed out the following: 'Submissive to the principles of Sharia, this Agreement shall be governed by and interpreted in accordance with the laws of England' see [2004] EWCA Civ 19 [1]. In contrast, see also *Islamic Investment Company of the Gulf (Bahamas) Ltd v Symphony Gems NV & Ors*, 2001 Folio 1226, slip. op. (EWHC (Comm) Feb. 13, 2002), The English High Court was asked to enforce a compensation of liquidated damages according to a contract. In the aforementioned case, the claimant (Islamic Investment Company of the Gulf) had entered into a Murabaha agreement with the defendant (Symphony Gems) under that the claimant was to provide a revolving purchase and sale facility to authorize the defendant to buy precious diamonds. Under the agreement, the defendant as a buyer, who describe and select the goods, which the claimant would then buy and instantly resell to the defendant with prior arranged profit margin for the claimant.

²⁵⁷ Under the Rome Convention of 1980, as applied in the United Kingdom during the Contracts (Applicable law) for the year 1990

²⁵⁸ Depending on Article 1.1 and Article 3.1 of the Rome Convention

²⁵⁹ see e.g. United Nations 12. 'It also occurs that the applicable law clause designates non-State rules such as *lex mercatoria*, or 'the general principles of international commercial law', or 'the UNIDROIT Principles for International Commercial Contracts'. Here again, the arbitrator must not hesitate to give effect to such clauses.'

Such confusion can be seen also in the earlier *Aramco* case,²⁶⁰ where the parties in the arbitration agreement agreed to apply *Sharia* law. However, the tribunal refused to apply *Sharia* law according to the argument because:

‘the regime of mining concessions, and, consequently, also of oil concessions, has remained embryonic in Moslem law and is not the same in the different schools. The principles of one school cannot be introduced into another, unless this is done by the act of authority. *Hanbali* law contains no precise rule about mining concessions and *a fortiori* about oil concessions’,²⁶¹

Arbitrators can decide the case according to the main sources of *Sharia* law through the use of the principle of *Qiyas* and *Ijtihad* and while not necessarily taking the role of government itself. The arbitrator is free to choose from the principles of *Sharia*, as it deems appropriate, based on *Ijtihad*. Therefore, *Sharia* law as a legal system is dependent on such sources and is therefore partly similar to the Common Law system.

3.3.3 The law applicable to the dispute if failing in choice of law

In fact, ‘the arbitrators’ selection of applicable laws will depend on an applicable international treaty, the law of the seat, or the conflicts rules of other interested states’.²⁶² The substantive law would be the applicable law if it has been chosen expressly by the parties. The substantive law of a foreign state or the law of the arbitration seat may be implicitly chosen as an applicable law. However, the applicable law may be different according to some opinion. Some national legislation and institutional rules require tribunals to apply the conflict of law rules of the state that they consider to be most closely connected to the dispute. The criteria to determine the most relevant law can be quite an extensive exercise, and may include consideration of the potential state of enforcement of the arbitral award, the state that would have had jurisdiction but for the arbitration, and the state of conclusion or performance of the contract.²⁶³

3.3.3.1 The Application of international law and trade usages

Most developed arbitration laws and many institutional rules provide that international arbitration tribunals either may or must consider trade usages to reach the award. Such laws provide the such trade usages are considered whether or not the parties have agreed to a choice of law clause.²⁶⁴ Other countries provide that such trade usages are considered unless contrary to

²⁶⁰ The *Aramco* Award 1958 cited in *Baamir* (n 24) 130–31; *Saudi Arabia v. Arab Am. Oil Co. (ARAMCO)*, 27 ILR 117 (1963). See also: Judge Stephen M. Schwebel, *The Kingdom of Saudi Arabia and Aramco Arbitrate the Onassis Agreement*, *Journal of World Energy Law & Business*, 2010, Vol. 3, No. 3 at 245.

²⁶¹ *Baamir* (n 24) 130–31.

²⁶² Born, *International Commercial Arbitration: International and USA Spectscmentary and Materials* 526–28.

²⁶³ Doug Jones, ‘Choosing The Law Or Rules Of Law To Govern The Substantive Rights Of The Parties’ (2014) 26 *Singapore Academy of Law Journal* 911, 911.

²⁶⁴ Born (n 22) 2664.; Art 28(4) of the UNCITRAL Model Law; Art VII (1) of the European Convention; United Nations 23; Art 39 (3) of the Egyptian Arbitration Law; Art 33 (3) of the Swiss Arbitration Law 2012; Art 21 (2) of

its law.²⁶⁵ However, such trade usages are difficult to determine practically in international arbitration with regard to issues of usury or interest. In commercial law, trade usages are considered as a secondary source after the principles of natural law, the general rules of justice, case law, and jurisprudence. These sources may vary from one legal system to another, and trade usages should not violate the rules of justice.

With regards to the application of international trade or commercial law, the practices of courts and arbitration tribunals highlights that:

'various authors have dealt extensively with the issue of interest, carefully examining national and international practices and often suggesting solutions that have been derived from or inspired by the practice and trends of international trade'.²⁶⁶

In private international law and arbitration, some countries may be directly linked to the provisions of CISG Convention 1980,²⁶⁷ and to the provisions of ICSID Convention 1965,²⁶⁸ and all the countries under this study are also subject to the NYC 1958. The ICSID Convention is directly linked to investment contracts and banking disputes that are related to investment, but it does not mention interest in its rules. ICSID rules are binding, and therefore have legal effect in the application of compound interest or higher rates of interest in the event of conflict of laws.²⁶⁹ The CISG Convention is related directly to the sale of goods, and sets the applicable law to the dispute with regards to compensation, interest and other rules if there is a conflict of laws, but it has not been able to meet the aspirations of different legal systems in different countries. This convention may conflict with other conventions and laws and may not adequately specify the applicable law, which also depends on whether the parties are within contracting states or not.²⁷⁰ There are also some who believe it may be applied to non-contracting states.²⁷¹ Although the CISG provides for compensation and interest in Articles 74 and 78, it does not refer to rates or

ICC Rules of Arbitration (2012); Art 35 (3) of UNCITRAL Arbitration Rules (2010); Art 28 of AAA International Dispute Resolution Procedures; Art 59 of WIPO Arbitration Rules; Art 22.3 of LCIA Arbitration Rules.

²⁶⁵ Art 38 (1)(c) of the Saudi Arbitration Law.

²⁶⁶ Giardina 129–30, 143–44 and 151.

²⁶⁷ The members from the countries under the study are only U.S. and Egypt.

²⁶⁸ The members of ICSID are UK since 1965, U.S. since 1965, France since 1967, Egypt since 1972, Kuwait since 1978, Saudi Arabia since 1979 and UAE since 1981.

²⁶⁹ See *Dei Peru Investments NO 1 v Republic of Peru*, 904 F Supp 2d 131 (DC 2012)

²⁷⁰ See the legal action in *ELDESOUKY v Aziz, No 11-CV-6986 (JLC) (SDNY Apr 8, 2015)*. 'Plaintiffs contend for the first time in their application for damages that the United Nations Convention on Contracts for the International Sale of Goods ('CISG') is applicable to the contract at issue in this action. The CISG is an international treaty governing contracts for the 'sale of goods between parties whose places of business are in different States ... when the States are Contracting States... Here, both the United States and Egypt are 'Contracting States.' The CISG has been described as 'a self-executing agreement,' meaning that, unless parties to a contract explicitly opt out of the CISG, it governs... Therefore, the CISG would seem to apply to the contract at issue in this dispute since Tasneem and Al-Yasmin are Egyptian companies while General Trade and Pyramid are American; however, by waiting until this late juncture to raise the applicability of the CISG, Plaintiffs have waived it.... the Court directs that judgment be entered against Aziz in the amount of \$1,237,301.36, with prejudgment interest running at the statutory rate of nine percent from the interest accrual dates listed below until the date judgment is entered.'

²⁷¹ Amin Dawwas and Yousef Shandi, 'Applicability of the CISG to the Arab World, The' (2011) 16 Unif. L. Rev. 813.

the accrual period. However, the articles of this convention are not compatible with some legal systems, particularly with regard to compensation and interest under *Sharia* or Islamic Arab laws.²⁷²

Assuming they do not conflict with the laws and that all states are subject to the provisions of this Convention, but that there is no unified opinion on the application of articles on compensation and the issue of determination interest.

[T]he issue of interest according to Article 78 has received different interpretations in both national courts and international arbitrations...In some cases, however, judges and arbitrators have considered that Article 78 affirmed the right of a party to be awarded interest, despite being silent on how it should be determined and that the issue therefore had to be solved according to the general principles of the CISG.²⁷³

However, there is one general view that interest is outside the scope of this convention, and that it 'could be awarded according to the applicable law chosen by the parties; or the applicable law determined by the court or the arbitration tribunal'.²⁷⁴ In addition, the application of international law may not be possible, due to: first, a lack of unified laws with regards to interest or compensation and existing laws that would be contrary to some countries' public policy or law; second, the relation between international arbitration and either private international law or public international law; and third, the nature of arbitration, the parties' autonomy, and the influences of law of the enforcement place.

3.3.3.1 The closest connection

Another approach that is applied to the choice of the substantive law by international arbitration tribunals involves selecting the law of the state that is most closely connected with the merits of the parties' dispute.²⁷⁵ Sometimes, the substantive law governing the contract is closely connected to merits of dispute, or may be the law of the arbitration seat.

There are three axes which may affect the choice of law and the most relevant connection. First, the parties, where they see the chosen law by them, is the most relevant connection to the issue of dispute. Second, the arbitrators or arbitration tribunal, where they see that the law of the arbitration seat is the most relevant connection to the merit of dispute. Third, the national courts in the enforcement country, where they see that national law is the most relevant connection to the subject of the dispute. Thus, it is possible to minimise the impact of the third issue, by reducing

²⁷² See Fatima Akaddaf, 'Application of the United Nations Convention on Contracts for the International Sale of Goods (CISG) to Arab Islamic Countries: Is the CISG Compatible with Islamic Law Principles?' (2001) 13 *Pace International Law Review* 1, 46–56.

²⁷³ Giardina 143–45.

²⁷⁴ Giardina 143.

²⁷⁵ Born (n 22) 2655.

extensive judicial review, and the second, by reducing the intervention of courts in the arbitration seat and the absolute power of the arbitrators.

The state that the substantive law is most closely connected to is often the enforcement country, where the applicable law will be enforced on a contract or dispute, or the country that decides whether the award is enforceable or not. The substantive law to the merits of dispute under such enforcement country is considered more than the freedom of parties that is considered substantive law of the contract, especially in the enforcement country, where the freedom of parties is limited to its interest, and the substantive law of this state.

The arbitrator's power to choose applicable laws is wider in the absence of any agreement between the parties, even if both parties may see his or her national law as the closest relevant to the dispute and that the place of the payment determines the interest.²⁷⁶ An arbitral tribunal authorised to directly select the substantive law to govern the parties' dispute may consider a variety of factors, including the nationality of the parties, the nature of the dispute or harm, the jurisdiction that will be most affected by the arbitral award, the place of contract creation and performance, the parties' intent, the place with the most significant contacts, and the terms of the contract itself.²⁷⁷ Although being difficult to predict, the law of enforcement country may be regarded as the law that has the closest connection to the merit of dispute, even if judicial review has been reduced on arbitral awards, due to the influence of public policy and arbitrability to the enforceability of the arbitral awards. The fact that there is often no or only minimal judicial review of the merits of arbitral awards does not mean in any way that arbitrators are free to disregard the law.

Born states that:

[T]his approach requires identifying what state is most 'closely connected' to a dispute – itself a potentially complex matter; then identifying what that state's conflicts rules are – again, not necessarily straightforward; and finally applying those conflicts rules to select a substantive law – requiring a further, potentially - complex analysis.²⁷⁸

However, it is not a complex analysis if states identify their conflict of laws rule and distinguish between the substantive and procedural laws. This approach should be applied in the absence of a unified law on usury and interest. However, it is true that choice of law rules, as well as substantive rules of law, must be applied with regard to the international character of the arbitration process and the underlying transactions.²⁷⁹ It is possible to determine the applicable

²⁷⁶ Giardina 141–42.

²⁷⁷ Tieder 400–01.

²⁷⁸ Born (n 22) 2654.

²⁷⁹ Born (n 22) 2657.

law of the contract after determining whether the contract is connected to or separate from the arbitration agreement, whether there is no explicit choice or not, and whether the parties have chosen their own terms or not.

3.3.3.2 As it deems appropriate

‘As it deems appropriate’ includes the choice of the applicable law to the contract or dispute in the interest of the parties’ wishes to use arbitration to settle the dispute. If the choice of applicable law is contrary to public policy, the arbitral award will not be given effect, as it would not be enforceable in the place of enforcement. Furthermore, an award may be refused recognition and enforcement if the potential conflicts between applicable laws have not been taken into account. This result would eliminate arbitration as a means of resolution, unless the arbitrator considers such disputes according to the parties’ agreement. The substantive law of the arbitration seat may reflect the parties’ intentions if the parties fail to choose the substantive law.²⁸⁰ Such assumption ignores that the parties’ choice of place of arbitration may simply reflect the parties’ considerations on neutrality or choice of the local law as the procedural law.

The arbitrator should take into the account all considerations in the absence of explicit law, where each law would impact on determining the applicable law, especially for interest, and any submissions by the parties as to the law should be taken into account. In this context, it suggests that it can do no harm and may do much to save the award, with respect to interest, from annulment or un-enforceability in certain circumstances if the award itself distinguishes clearly between interest in the pre-award and post-award periods.²⁸¹ It is clear that the law applicable to the contract and merit of the dispute is considered the important factor in determining the ability of the tribunal to award interest.²⁸²

If the parties select the law applicable to the dispute, the arbitrators will be bound by the application of the law of the contract or those conditions that included interest.²⁸³ These conditions may be included in the contract, or the arbitration agreement, or both. The arbitrator has no choice but to give effect to these conditions under the legitimate expectations of the parties and respect the terms of the parties’ agreement according to the nature of international arbitration, international contract law, and to ‘support[s] a degree of flexibility in the application of this distinction’.²⁸⁴ If the parties fail to choose the applicable law or there is no reference to interest or damages, there is confusion whether the arbitrators determine such a matter according to: the

²⁸⁰ Giardina 136.

²⁸¹ Hunter and Triebel 8.

²⁸² Born (n 22) 2653; Hunter and others 8.

²⁸³ Giardina 136.

²⁸⁴ UNITED NATIONS, ‘UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT: The Law Governing the Merits of the Dispute’ 13.

conflict of laws rules deemed applicable or appropriate,²⁸⁵ the direct choice by the arbitrators of the rules governing the contract,²⁸⁶ on the basis of arbitration rules,²⁸⁷ or in accordance with the absolute freedom of arbitrators.²⁸⁸ However, through the identification of the applicable law, the substantive and procedural rules may contribute to the removal of this kind of confusion. Born observes that the distinction between substantive and procedural issues is elusive even within national legal systems.²⁸⁹ However, if we distinguish between substantive and procedural law of each legal system with regards to usury or interest, such confusion will be removed, specifically with regards to the enforcement of foreign awards in the enforcing state. According to the freedom of the parties, the arbitrator shall apply the applicable law to the contract containing the explicit conditions. In addition, applying such conditions as the freedom of the parties is one of the substantive rules of contracts unless such freedom conflicts with the substantive law under the applicable law. These conditions are necessary to determine the scope of the agreement or the authority of the arbitrator, and overriding these conditions or awarding beyond the scope of the agreement may cause the award be unenforceable due to a lack of arbitrability.

The arbitrator is free to decide 'to undertake the search, to decide how to go about determining the existence or otherwise of an implied intention'.²⁹⁰ Consequently, it does not seem unreasonable for arbitrators to take into account the implied wishes of the parties. The freedom of arbitrators to choose does not mean that they have an absolute freedom, but remain obligated to select the conflicts rules that are 'appropriate' in light of the procedural law of the arbitration and the parties' arbitration agreement. The authority of the arbitrator is limited to the parties' autonomy, the substantive and procedural rules of the arbitration agreement, and the applicable law of the contract. Born notes that 'although frustration with contemporary choice of law rules is understandable, 'direct' application of national law is not an appropriate response'.²⁹¹ However, it is an appropriate response if it would achieve the goal of the NYC and avoid the refusal of the enforcement of foreign awards, but it does not in any event directly apply the national law of the arbitration seat.

Unless there is an express law which would give effect to the applicable law, the arbitrators are free to choose the rule or rules to apply if the parties fail in choice of law.²⁹² The arbitrators must select a conflict of laws rule from among various possible conflicts systems to be

²⁸⁵ Giardina 137.

²⁸⁶ Giardina 138.

²⁸⁷ Giardina 140.

²⁸⁸ See s49 of the Arbitration Act, 1996.

²⁸⁹ Born (n 22) 2667.

²⁹⁰ United Nations 14.

²⁹¹ Born (n 22) 2646.

²⁹² UNITED NATIONS, 'UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT; The Law Governing the Merits of the Dispute' 17.

applied. They have the power to apply the appropriate law in the absence of any indication of agreement by the parties. However, in event that there is such an agreement, they shall apply their choice unless it is contrary to the law or mandatory rules or public policy of the relevant law.

The method most commonly used to resolve interest claims when the contract is silent or ambiguous on the subject is for the arbitrator to select and apply a pertinent national substantive or procedural law. Unfortunately, in international arbitration proceedings, the process of ascertaining a national law to be applied to the interest claim is particularly complex. Further complications arise when choosing a law to be applied to an interest claim. There is a lack of unanimity concerning whether procedural or substantive law governs the questions of whether an arbitration tribunal has the authority to decide in states having a connection with the parties' dispute, an international treaty, or an international arbitration institution. Unfortunately, there is no consensus on the method of awarding interest in international arbitrations. In resolving an interest claim, arbitrators have to look to the agreement for guidance, select a national law to govern the issue, rely on general principles of international law, or simply base decisions on what is considered fair and reasonable under the circumstances.²⁹³

3.3.3.3 Applicable law from the conflicting laws

There are a number of relevant factors which give effect to the applicable law to the contract, such as conflict of laws, lack of uniform laws, and lack of clarity in international conventions. Such conventions can give rise to greater misunderstanding and confusion in interpretations because there currently appears to be no consensus as to which rules should be applied by the arbitrators to identify the applicable law and award interest, and furthermore how it determines the accrual period and the rates of interest. First of all, the arbitrators should determine the applicable law by applying the relevant connection theory through analysis of the contract and the arbitration agreement, whether such an agreement is a clause or a separate agreement. Second, they should identify the express laws or choices made, and whether the parties have identified the arbitration seat and the law of the arbitration agreement. The parties in some cases may appoint arbitrators before selecting the seat of the arbitration,²⁹⁴ and sometimes the arbitration centres make such appointments. It is necessary to appoint the arbitrators in advance to avoid the legal effect of Art V (1)(b), which is also required under many jurisdictions.

The express law that governs the contract is the law governing the validity of the contract. Such terms must not be contrary to the substantive law of the governing law, unless otherwise

²⁹³ Gotanda, 'Awarding Interest in International Arbitration' 40.; Art 39 (2) of the Egyptian Arbitration Law.

²⁹⁴ Art 20 of the UNCITRAL Arbitration Rules 2013; Article 18 of the Model Law; Art 16 of the Swiss Rules; s3 and 14 of English Arbitration Act etc. Art 22 of the Egyptian Arbitration law, apply *lex causae*, or otherwise the arbitral tribunal would determine the law that it deems to have the closest connection to the dispute

stated. In contrast, the implied laws take the same rule of law as the explicit law in terms of applicable law. However, if there is no explicit law which governs the contract and the contract is connected to the arbitration agreement, the law governing the arbitration clause is the law that is applicable the contract and the dispute under the theory of the closest connection. On the other hand, if the contract is connected to the arbitration agreement and there is no law governing the arbitration clause, the law of seat of the arbitration is the law applicable to the contract because it is the law governing the arbitration.

In arbitration, the arbitrators have the same power as those of the judges in a national court to consider the applicable law to the contract.²⁹⁵ If the contract is separate from the arbitration agreement, the parties have expressly chosen the law governing the arbitration agreement, and if there is no explicit law governing the contract, then the law of the arbitration agreement is the law that is applicable the contract and the dispute under theory of the closest connection and its legal effect. If the law of the arbitration agreement addresses interest and compensation matters, it resorts to the national law of the law of the arbitration agreement. If there is no law governing the arbitration agreement and the parties have expressly chosen the arbitration seat, then the law of seat of the arbitration is the law applicable to the contract because it is the law governing the arbitration under Art V of the NYC. However, failing any indication of the arbitration seat or the chosen law of the arbitration agreement, the arbitrators consider the contract and dispute with almost absolute freedom to determine the applicable law under the theory 'as it deems appropriate', taking into account the wishes of the parties. As a result, the applicable law also governs the validity of the contract and the merit of dispute under the terms of the parties. Thus, when the arbitrators apply the law selected by the parties, whether express or implicit, terms in the contract limit the role of judicial review of arbitral awards.²⁹⁶ The arbitral award is binding to the parties and the enforcement country unless it is contrary to its public policy or it is non-arbitrable.

3.4 Conclusion

The national courts, whether in the arbitration seat of the chosen law or of the enforcement place, would conflict with each other regarding the legality of interest rates and the parties' terms and conditions in this regard. In addition, a conflict arises between the law applicable to the arbitration agreement and the law applicable to the dispute. However, neither the law of the arbitration seat nor the law applicable should have an effect on the applicable law to the dispute if that has been chosen expressly by the parties. The law applicable to the arbitration

²⁹⁵ Born (n 22) 2619–20.

²⁹⁶ Born (n 22) 2624–25.

agreement would be the law that determines the authority of the arbitrator to award interest, to apply a specific law or to determine the applicable law to dispute where there are conflicts of law. The law of the arbitration seat would apply automatically where the substantive and procedural laws are concerned, and by implication where no law has been expressly chosen. In case there is none indicated, the matter is determined by the arbitrator as it deems appropriate, taking into account the parties' agreement.

A confusion arises regarding the determination of interest laws, whether the issue is substantive or procedural and whether or not punitive damages are allowed; and there is confusion in interpretations of interest under some jurisdictions regarding the relation between compensation and usury and illegal interest rates. Due to the diversity of the interest laws, the applications and interpretations of these laws, and the court interventions in the application of the chosen law, it is difficult to determine whether the subject of interest falls into the scope of substantive or procedural matters. Furthermore, complications may arise from this subject in relation to compensation, loan, late payment and damages, especially under *Sharia* law. Reflecting on these complications in the context of the enforcement framework of the New York Convention, a closer examination of their impacts on arbitrability and public policy would be beneficial in providing further understanding of the issues involving interest.

Chapter 4. Interest and Contracts Under *Sharia* Law and Positive Laws

4.1 Introduction

Awarding interest is a norm in most jurisdictions, however, *Sharia* law views this issue differently despite interest being an important matter in commercial laws due to its interpretations, applications and influences on the parties and on the settlement of the dispute. This can be seen more clearly in international commercial arbitration involving Saudi Arabia due to conflicts of laws with regards to such matters. There are many arguments among jurists, experts, economists and researchers with regards to the concept of interest and its practices that show the expected influences on this concept. Additionally, economic and political conditions have also contributed to the volatility of this concept.

These differences exist and continue to create conflicts between laws even under a single legal system and between positive laws. Interest varies from one country to another according to its law or the legal system it is based upon. This chapter will address the concept of interest and its relationship to usury under different laws, giving consideration to contracts related directly or indirectly to interest. It will also examine different types of interest, and interest with regards to compensation for damage or delay in payment or delivery, for breaches of contract, or for punitive damages. It will also address principles of contracts such as party autonomy and examine their influences on laws and contracts.

Under some legal systems, contracts that contain interest would be considered null and void, and would therefore lead to non-arbitrability. The differences between the judicial authorities in arbitrable matters may also affect the functioning of international commercial arbitration,²⁹⁷ either at the enforcement of the arbitration agreement stage or the stage of enforcement of the award. The awarding of interest would be considered unenforceable in such jurisdictions if it is contrary to public policy. It is important to understand the reasons for refusing the award of interest in these countries and legal and illegal interest, substantive and procedural laws with regards to interest, and whether such a choice would be considered non-enforceable on the NYC's grounds of refusal or not. The importance of this chapter lies in defining interest under different laws or legal systems, which leads to avoidance of further disputes, conflicts of law, misunderstandings and confusion between arbitrators, parties and judges. In addition, it paves the way to dealing with conflict of laws and influences of interest on enforcement. Therefore, it is

²⁹⁷ Kutty (n 25) 565, 602.

necessary to understand the concept of interest under different laws such as *Sharia* and other positive laws.

4.2 Interest and Usury

4.2.1 *Conflicts in the definition of interest and usury*

Despite the large number of attempts to give a clear definition of interest and usury, the difference between these terms cannot be distinguished.²⁹⁸ In Latin the word of *usura* (use) means gain of anything by contract whether money or any other thing above the capital for the use of this money.²⁹⁹ Hence, usury was the money paid for the use of borrowed money.³⁰⁰ In old English law, usury meant 'interest of money; increase for the loan of money; a reward for the use of money'.³⁰¹ Usury was unlawful 'where more is asked than is given',³⁰² and 'letting money out at interest, or upon usury, was against the Common Law'.³⁰³

The theory of interest in the Middle Ages slowly developed and the Latin word *intereo* 'to be lost' developed into the modern term 'interest'. Interest was not for profit but for loss.³⁰⁴ It was considered as compensation due to the loss which the creditor had incurred through lending.³⁰⁵ This concept came from Roman law, which gave more consideration to the lender as an injured party rather than the borrower, and the compensation was considered to be damages within a broad conception, including profit that might have made by the lender.³⁰⁶

In modern law, usury means unlawful interest, compensation paid for the use of money borrowed beyond the legal interest rates, either directly or indirectly.³⁰⁷ Brook observes that 'the term usury is widely taken to mean 'excessive interest' (which is never defined) or illegal interest'.³⁰⁸ Thus, it is an unlawful contract to give and receive the sum with an exorbitant

²⁹⁸ Mews and Abraham 1; Sidney Homer and Richard Sylla, *A History of Interest Rates* (Wiley 2011) 71.

²⁹⁹ See Thomas Edlyne Tomlins, *The Law-Dictionary: Explaining the Rise, Progress and Present State of the British Law: Defining and Interpreting the Terms Or Words of Art, and Comprising Also Copious Information on the Subjects of Trade and Government* (Payne 1820); see also Homer and Sylla.

³⁰⁰ Tomlins; Homer and Sylla.

³⁰¹ Henry Campbell Black, *A Law Dictionary Containing Definitions of the Terms and Phrases of American and English Jurisprudence, Ancient and Modern ...* (Lawbook Exchange 1995) 1192.

³⁰² Homer and Sylla 71.

³⁰³ Tomlins.

³⁰⁴ Homer and Sylla 71 'Compensation for loans was not licit if it was a gain to the lender, but become licit if the compensation was not a net gain, but rather a reimbursement for loss or expense.'

³⁰⁵ Homer and Sylla 71.

³⁰⁶ Homer and Sylla 71 'It was often a compensation or penalty for delayed repayment of a loan. Such damages might arise (a) when guarantors of a loan were forced to borrow to make good and thus to pay usury; they could recapture the usury as damages; (b) when a loan was not repaid at the agreed time, and a penalty for delay might be charged, the latter case penalties sometimes ran to double the sum lent.' He gave an example for that.

³⁰⁷ Black 1192; Tomlins.

³⁰⁸ 'The actual definition of the term is, as the Oxford English Dictionary specific; "the fact or practice of lending money at interest".' see Yaron Brook, 'The Morality of Moneylending: A Short History' (2007) 2 The Objective Standard 9.

increase, or to make a profit at an unreasonable rate beyond what is allowed by the law.³⁰⁹ Usury is prohibited by Civil Law,³¹⁰ such as French law, and some interest is prohibited by *Sharia*.

Monroe emphasises that it is agreed by good authors that the origin of the word of 'usury is not for taken the thing but for the use of thing', thus, he observes that the 'demand payment for the use of anything or for the principal' in case of a loan contract, is unjust, and is inherently evil.³¹¹ This view is likewise the view of *Sharia* law in some aspects. Monroe says that usury is not like trade in commodities in which an equivalent is always given and received. In usury, despite that the use of the money gives the user a greater advantage for a time, the interest continues until the principal is paid in full, thus in such case if the usury was multiplied it would mean that all property of the debtor would be given to the lender.³¹² It is the same in the *Quranic* approach which states where Allah has permitted trade and prohibited usury.³¹³ However, usury may be present in some commodities under *Sharia* law.

Usury is to sell what does not exist and clearly leads to inequality, and consequently it is contrary to justice.³¹⁴ Moreover, usury is contrary to nature³¹⁵ and a blight on society, although some authors argue that usury is just compensation for the lawful costs incurred in any loan.³¹⁶ However, interest on a loan is not illegal in most jurisdictions, but usury, which is charging above the legal interest, is outlawed by most jurisdictions. Certainly, this is the view of some jurisdictions, but not all or even the majority. Some authors find that the concept of interest means just compensation, and that interest is compensation for actual loss or forgone opportunities of profit, which requires charging interest.³¹⁷ This reflects the concept of interest in Roman law during the Middle Ages, though usury is not only compensation in a broad sense, but also interest-based debt is compensation in a broad sense. It is not compensation if there is no actual damage. All this is in an attempt to find a clear definition of usury and reconcile the idea of usury in law and economics in terms of the principles of justice and the economic interests.

³⁰⁹ Black 1192; Tomlins.

³¹⁰ Calvin Elliott, *Usury: A Scriptural, Ethical and Economic View* (Library of Alexandria 2007) ch XIX.

³¹¹ See Monroe 109 he gives three reasons for example double compensation for the same thing, with some comments.

³¹² Monroe 111.

³¹³ *Quran* 2:275.

³¹⁴ Leszek Niewdana, *Money and Justice: A Critique of Modern Money and Banking Systems from the Perspective of Aristotelian and Scholastic Thoughts* (Taylor & Francis 2015) 54.

³¹⁵ 'to make money by usury is exceedingly unnatural' Niewdana 55; 'usury is especially contrary to nature.' for some comments see Monroe 111.

³¹⁶ Mews and Abraham 12.

³¹⁷ See Niewdana 58–59, 64–71. The author distinguishes between interest and usury.

4.2.1.1 The real and closer definition of interest and usury

Interest was at first a legal term concerning the rate increase that is allowed by the law, however the legal rates greatly vary and are changed from time to time by the law of the states.³¹⁸ Monroe argues that what is in Civil Law is compensation and not usury, usury should not be universally prohibited due what may happen only rarely, and the law should be adapted accordingly. He notes that they do not consider usury, or what is meant by laws limiting usury, as a result of both of ignorance of the law and the lack of practical experience.³¹⁹ Actually, charging reasonable interest is not prohibited, which is not usury in most jurisdictions except *Sharia* law.

The modern usage of usury is limited to an unreasonably high interest rate that is prohibited by the law, thus, usury covers interest while interest refers to what is allowed by the law in different countries.³²⁰ As a result, the two words usury and interest reflect each other, every usury can be interest but not every interest would be usury and what may be usury in one country is only interest in another. Blackstone emphasises 'when money is lent on a contract to receive not only the principal sum again, but also an increase by way of compensation for the use, the increase is called interest by those who think it lawful, and usury by those who do not'.³²¹ Such view is said to reflect somewhat the view of the English law compared to *Sharia* law. However, it may not represent the whole truth simply because there is a middle approach, where charging above the legal interest rate is the usury. In brief, in some countries charging interest above the legal interest rate is usury under different percentages, as will be mentioned.

To summarise, interest is money paid regularly at a particular rate for the use of money lent, or for late payment of a debt. Usury is charging excessive interest. It is '... [taking] a greater sum for the use of money than the lawful interest'.³²² The difference is very clear, although the dividing line may not be and may vary from place to place. There is who do not want there to be a difference between the two because for them such confusion serves a broader purpose. However, 'the usury law is complex and is riddled with so many exceptions that the law's application itself seems to be the exception rather than the rule'.³²³ Thus, 'the plain language of the constitutional

³¹⁸ Elliott XIX.

³¹⁹ Monroe 114–120.

³²⁰ 'if a state should forbid the taking of any increase on loan, then all increase would be usury, and there could be no interest; or if a state could repeal all laws limiting the exactions of increase, then there would be no usury in that state.' See Elliott XIX.

³²¹ William Blackstone and others, *Commentaries on the Laws of England: In Four Books; with an Analysis of the Work. With a Life of the Author, and Notes: By Christian, Chitty, Lee, Hovenden, and Ryland: And Also References to American Cases* (WE Dean 1838) 372; see Jeremiah O'Callaghan, *Usury: Funds and Banking, Monopoly, Forestalling, Traffick, Gallican Liberties, Graves, Anatomy* (the New York Public Library 1856) 217; see also Elliott.

³²² Born, *International Arbitration: Cases and Materials* 1072; Gary B Born, *International Arbitration: Cases and Materials* (2nd edn, Kluwer Law International 2015) 1137.

³²³ *Bisno v. Kahn*, 225 Cal. App. 4th 1087, 170 Cal. Rptr. 3d 709 (Ct. App. 2014) [1098].

usury provisions does not permit a construction that prohibits the receipt of interest in excess of the statutory rate from a judgment debtor'.³²⁴

4.2.2 *Interest rate, simple and compound interest, and period*

Usually interest provisions are included either in the arbitration law governing the arbitration agreement or in the civil codes or civil procedural codes, or both, governing such issue. The law of each country can be chosen either as a law governing the arbitral agreement or as a law governing the merits of dispute. In addition, each country would take place either as a seat of arbitration or as a place of enforcement of the arbitral award. Thus, the law of each country would give effect in the international commercial arbitration with regards to disputes containing interest.

4.2.2.1 **England**

In England, there is no usury law, but there are written provisions in relation to late payment and compensation, though not enough to clarify the rates and other anticipated problems. It could be based on common law. However, in the English Arbitration Act 1996, the parties are free to agree on the arbitrators' power to award interest, for any period,³²⁵ in order to avoid misinterpretation in some respects, with no limit rate even compound interest. The date of the interest is determined under the parties' agreement, under the arbitrators' power, or under the applicable law to the contract. Such provision of Act will be applied to the loan contract and other contract related to interest. It may be applied by arbitrators in the cases where no expressed choice of law was reached between the parties. However, it may be in conflict with either the foreign seat of arbitration or the foreign place of enforcement. Under the English law, there are many laws govern the contract and the terms with regards to interest. However, according to the report No 287 issued by the Law Commission, it states:

Pre-judgment interest on debts and damages may be awarded in many different ways, at a variety of different rates. The statutory provisions alone range from 0.5% below base to 8% above base [...] Compound interest is awarded routinely under contracts. For example, contracts for bank loans, mortgages, credit or store cards will almost always include provisions for compound interest. Compound interest may also be awarded in arbitration. However, in the absence of specific contractual conditions or trade usages, the courts rarely award compound interest...An alternative approach is to link court interest rates to the bank base rate (or occasionally to LIBOR). This is the usual approach in the Commercial Court, where case law suggests a rate of 1% over base, which is thought to reflect

³²⁴ Ibid at [1103]

³²⁵ According to s49 of the Arbitration Act, 1996; see Lord Mustill and Stewart C Boyd, *Commercial Arbitration* (2nd edn, Butterworths 2001) 331–334; see also Joe Tirado/ Winston & Strawn LLP, 'England & Wales - International Arbitration' (*global legal insights*, 2015) 6 <<http://www.globallegalinsights.com/practice-areas/international-arbitration-/global-legal-insights---international-arbitration-1/england-and-wales>> accessed 20 October 2015 'The default position under the Act is that the tribunal may award simple or compound interest at such rates and with such rests as it considers appropriate, up to the date of the award and from the date of the award to the date of payment, on: the whole or part of any amount awarded in respect of the principal claim; and any award as to costs.'

the actual cost of borrowing among commercial parties. Other courts have also adopted this approach in cases of economic loss [...] It is common for creditors to receive simple interest at 8%.³²⁶

4.2.2.1.1 The power of the arbitrator

Under English law, whether as the law of the seat of arbitration or the law governing the arbitration, the arbitrator has power to award interest unless the parties stipulate otherwise. In case the place of enforcement is England, 'the power to award statutory interest may be excluded by a contractual provision which provides for interest at a different rate or for no award of interest',³²⁷ '[t]he parties, it has to be assumed, have deliberately agreed to give jurisdiction to an arbitrator to decide on the rate of interest, including interest for the period between the award and payment of the amount awarded'.³²⁸

4.2.2.2 United States

The U.S. has the Uniform Commercial Code and U.S. Laws, Codes and Statutes, and each state may have its own law that is different from the other state. Additionally, the Federal Codes and Statutes, impact on state law regarding interest, but that Federal Arbitration Act does not mention the awarding of interest. In the U.S., there are trends for usury limits in many jurisdictions, though each state has its own law which may conflict with one another. For example, in Rhode Island the allowable rate of interest is 21% and where the court found that the rate was exceeded,³²⁹ the award was unenforceable due to a violation of the usury law.³³⁰ Thus, the lack of uniformity with regards to interest rates leads to conflicts of law between the states of the U.S. with regards to the law applicable to the merits of the dispute. Whether awarding interest is a substantive or procedural matter and whether there is a violation the law is considered against public policy or non-arbitrability. Martin and Green observe that in U.S:

'...interest to be a substantive issue'.³³¹

However, violation interest rates or charging above the allowable rate is substantive issue in some states and such rate is different from one state to another. The U.S. Court of Appeals provides that 'violating usury laws in numerous states by charging an interest rate above statutory limits and not registering as a loan institution'.³³²

³²⁶ The Law Commission (LAW COM No 287, 'PRE-JUDGMENT INTEREST ON DEBTS AND DAMAGES' (2004) 17–20 <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/228650/0295.pdf>.

³²⁷ *Yukos Capital SARL v OJSC Rosneft Oil Co* [2014] EWHC 2188 (Comm) (Lord Grabiner) [75].

³²⁸ *Ibid* (Megaw LJ) [76].

³²⁹ *NI'ONE, LLC v. Potomac Realty Capital, LLC*, 84 A.3d 800 (R.I. 2014) at [804].

³³⁰ *Ibid* [810].

³³¹ Craig C Martin and Jason J Green, *International Arbitration and Litigation* (Jenner & Block 2014) 44.

³³² *Pang v INTERNATIONAL DOCUMENT SERVICES BT - UT* (2015) 2015 63 [28].

The substantive law governing the dispute will usually decide the interest rate and the period. U.S. Court of Appeals, Fifth Circuit under the Louisiana law in *Norman P. Hymel v. UNC, INC.*, directly considered the parties' agreement;

'Based on this language in the note, the district court set the post-judgment interest at 9% per annum.' ... 'a standard rate of post-judgment interest, the parties are free to stipulate a different rate, consistent with state usury and other applicable laws'... "the contract governs the rate of interest."³³³

However, the courts may refuse to enforce the awarding interest if it is punitive or otherwise contrary to the applicable or state usury law, vitiates the contract,³³⁴ or is non-arbitrable.³³⁵ Each state has its own law despite the presence of the Uniform Code. In a recent case, a conflict arose between New York law and California law with regards to interest rate and the applicable law.³³⁶

Where 'that the Credit Agreement is unenforceable because it violates California's usury laws...the Law Firm is located in California, Hamilton is located in New York, and all of the contracts are governed by New York law.'³³⁷

Under the conflict of laws analysis, the court has applied the New York law including a usury law.³³⁸ Thus, each state has its own law with regards to the illegal interest rate and the cap of such interest is different from one state to another. In addition, it may be considered as a substantive issue in one state such as California State and procedural in another, let alone the possible involvement of different states. For example;

'Under California law, interest accrues at a rate of ten percent from the date of the arbitration award resolving the contractual dispute, to the date of judgment in this Court affirming the arbitration award.'³³⁹

While different approaches are held by various states, however, under the U.S. Code, such interest rate is considered under the law of the state in which the court is held and the federal statutory interest rate on the confirmed award will be imposed unless the parties agreed to apply a higher rate until the full amount is paid.³⁴⁰ The period of the pre-award is governed by the chosen

³³³ *Norman P. Hymel v. UNC, INC.*, 994 F.2d 260, 266 (5th Cir 1993) [28].

³³⁴ See *Pang v. INTERNATIONAL DOCUMENT SERVICES BT - UT* [28].

³³⁵ *Hayes v. County Bank*, 713 N.Y.S.2d 267 (N.Y. Sup. Ct. 2000) 'held that the FAA permits setting aside arbitration agreements on unconscionability grounds, and a payday loan scheme with such a contract was found to be unconscionable'; *Party Yards, Inc. v. Templeton*, 751 So. 2d 121 (Fla. Dist. Ct. App. 2000) 'held that a usury violation is not arbitrable; it is a matter for the courts' (See Chapters Five and Six)

³³⁶ See e.g. *Hamilton Capital VII, LLC v. Khorrami, LLP*, 2015 N.Y. Slip Op 51199 (Sup. Ct. 2015).

³³⁷ *Hamilton Capital VII, LLC v. Khorrami, LLP*, 2015 N.Y. Slip Op 51199 (Sup. Ct. 2015).

³³⁸ 'In New York, however...preclude courts from questioning a validly agreed-to choice of law clause. Hence, even if a California court might..., deem the parties' New York choice of law clause unenforceable, this court may not do so. The court must apply New York law, including New York's usury laws.' See *Hamilton Capital VII, LLC v. Khorrami, LLP*, 2015 N.Y. Slip Op 51199 (Sup. Ct. 2015).

³³⁹ In *WICHARD v Suggs*, No. 1:15cv3 (JCC/TCB) (E.D. Va. Mar. 24, 2015).

³⁴⁰ 'Such interest shall be calculated from the date of the entry of the judgment, at a rate equal to the weekly average 1-year constant maturity Treasury yield, as published by the Board of Governors of the Federal Reserve System...' 28 U.S. Code § 1961(a). See *Meaux Surface Prot, Inc v Fogleman*, 607 F.3d 161, 173 (5th Cir 2010); *Johnson v Riebesell (In re Riebesell)*, 586 F.3d 782, 794 (10th Cir 2009); see also *Fid Fed Bank, FSB v Durga Ma Corp*, 387 F.3d 1021, 1024 (9th Cir 2004); *Carte Blanche (Singapore) Pte, Ltd. v Carte Blanche Int'l, Ltd*, 888 F.2d 260, 268-70 (2d Cir 1989); *Tricon Energy Ltd v Vinmar Int'l, Ltd*, 718 F.3d 448, 458 (5th Cir Tex 2013).

state law, while the post-award is subject to the federal law unless otherwise agreed (see Chapters Five and Six).

4.2.2.3 France

In France, the situation is different where the law applicable to the contract may determine the legality of interest rate. The interest rate fixed by statute, which is revised every year and should apply unless a different rate is required to be applied by the agreement. However, usury is banned in France, so the total amount of interest should not exceed one third of the principal amount, it is considered a violation of the Statute of usury in France.³⁴¹ Usury law is considered mandatory law in France, as they have applied to domestic transactions, and in this case may apply French usury statute if the court has found it as part of mandatory laws.³⁴² In France there is no mention of awarding interests in the Code of Civil Procedures.

Furthermore, it is also considered a criminal offence and that the lender is subject to sanctions including imprisonment and fines, due to it is contrary to the ordinary principles of justice etc.³⁴³ The legal ambiguity surrounding the usury and such restrictions have driven the French corporates to borrow from financial centres outside of France, and borrow from the foreign market such as London or New York market, thereby the interest rate is in line with prevailing market rates, is considered legal.³⁴⁴ French usury rules do not specify a usury reference rate for large-scale corporate loans or for loans denominated in foreign currency. Such a reference rate is essential to put parties on fair notice of the limits of a statute that imposes criminal sanctions. As a result, charging illegal interest rate is a breach of the substantive mandatory law in France, and to apply the usury law to any loan contract is subject to scrutiny of the French courts.

4.2.2.3.1 The international concept theory

However, in international arbitration, under the French concept of “international”, a usury law may be interpreted as an international mandatory provision.³⁴⁵ The Court of Appeal in Paris held if the interest rates do not exceed the threshold of usury in foreign jurisdictions, it will not constitute a violation of French international public policy, which means the acceptance of interest rates operated in foreign jurisdictions.³⁴⁶ In international arbitration, France is relying on the

³⁴¹ Law No. 93-349 of July 26, 1993, as Article L. 313 et seq. of the French Consumer Code; see also Arvind Ashta, ‘French Legislation And The Development Of Credit Availability For Microenterprise’ 5.

³⁴² See Eric Cafritz and Omer Tene, ‘Article 113-7 of the French Penal Code: The Passive Personality Principle’ (2003) 41 Columbia Journal of Transnational Law 585, 589.

³⁴³ See Cafritz and Tene 589; See also Attuel-Mendes and Ashta.

³⁴⁴ ‘Conflict of Laws in International Loans to French Corporations: The Usury Question’ (2008)

<<http://corporate.findlaw.com/finance/conflict-of-laws-in-international-loans-to-french-corporations.html#sthash.ae1JXo4y.dpuf>> accessed 11 October 2015.

³⁴⁵ See e.g. Cafritz and Tene 589.

³⁴⁶ *Holding Company Iro-v. Setilex Society*, C.A. Paris 1, June 9, 1983, Journal of arbitration 1983, 497, M. Vasseur, holding: “it is not shown, or even alleged, the excess of which is make it higher than those in foreign countries agreed

“international” concept, where neither the law applicable to the arbitral agreement, the law applicable to the dispute, nor the enforcement of the foreign arbitral award should contrary to the international public policy, the further examined in Chapters Five and Six.

4.2.3 *Interest under Sharia law*

Interest is stated in the main sources, the *Quran* and *Sunna*. However, these sources need interpretation to be applied in modern trade. Since the beginning of Islam or pre-Islam until the current time, it has been difficult to agree on the meaning of *Riba* in *Sharia* law from religious perspective, consequently, it is the researcher’s intention to address and clarify the issue of interest under *Sharia* as a legal system and a source of legislation in some countries.

4.2.3.1 *The concept of Riba*

In Arabic, the word *Riba* means extra, increased or additional interest,³⁴⁷ which is similar to the English concept of usury. It does not mean a just increase but means multiplexed or greater interest. However, it is related not to the loan contract it is also related to debts and sale contract. This does not necessarily mean that any increase is prohibited, but the prohibition reflects the illegal interest under *Sharia* law according to the type of contract. This definition is derived from the *Quran*, *Sunna* and the Arabic language that are all unanimously accepted by Islamic scholars. *Riba* is expressly prohibited under *Sharia* law.³⁴⁸ Despite that, it is still ‘a contentious issue in Islamic jurisdictions’³⁴⁹ and is considered as one of the most important and most discussed issues in Islamic law in the modern period in terms of its applications, but not its meaning.

All Islamic scholars agree on the prohibition of *Riba* as one of ‘*Usul al Fiqh*’, such compatibility reflect the meaning of *Ijma*, but they do not agree on ‘*Furu al Fiqh*’. This controversy is because of a misinterpretation of *Riba* and the result of differences between schools of jurisprudence in the effective cause (*il’lah*) of *Riba* by applying analysis and analogy (*Qiyas*), despite using same sources. This disagreement has led to a variance in its effective cause since the Middle Ages, which causes a variance in opinions and judgments as a result. The difference is more clearly apparent in the present with the development of financial transactions and new types of contracts, transactions, securities, and various compensations. That conflict between economy, law and religion has also influenced the concept of *Riba* in *Sharia* law just like other

rate, and in conditions that violate international public policy under French private international law”. Cited in ‘Conflict of Laws in International Loans to French Corporations: The Usury Question.’

³⁴⁷ See Baamir (n 24); Abdel-Rahman Yousri Ahmad, ‘Riba, Its Economic Rationale and Implications’ (*Institute of Islamic Banking and Insurance*) <http://www.islamic-banking.com/iarticles_8.aspx> accessed 8 September 2015; M Umer Chapra, ‘The Nature of Riba in Islam’ (2006) 2 *The Journal of Islamic economics and finance* 7, 1; see also Kutty (n 25) 604.

³⁴⁸ ‘...Devour not usury, doubled and multiplied; ...’ See *Quran* 2:275,276&3;130; Some Hadiths cited in B Kettell, *Frequently Asked Questions in Islamic Finance* (Wiley 2010).

³⁴⁹ See Kutty (n 25) 604.

positive laws.³⁵⁰ However, *Sharia* law might be more flexible with regard to this aspect, in terms of the rules and principles of *Sharia* which can be applied beside the main sources after extracting the effective cause 'il'lah' and applying analogy. Therefore, some of concepts of *Sharia* may be steadfast, with some hyperbole or leniency.

4.2.3.2 The Six Commodities

The primary sources of *Sharia* law prohibit *Riba*, which can be found directly in several texts such as the *Quranic* text 'Devour not usury, doubled and multiplied';³⁵¹ the *Hadith* text 'all contracts of *Riba* of the pre-Islamic period are null and void. The first contract of *Riba*, I am cancelling, is that of Abbas bin Abdul Muttalib';³⁵² and in the *Hadith* text:

Gold is to be paid for by gold, silver by silver, wheat by wheat, barley by barley, dates by dates, salt by salt, like by like, payment being made hand to hand. He who made an addition to it, or asked for an addition, in fact dealt in usury. The receiver and the giver are equally guilty.³⁵³

In addition, in the *Hadith* text that 'any loan [which] draws a benefit is *Riba*',³⁵⁴ refers to the loan contract.

Islamic scholars agree that *Riba* is prohibited under the main sources according to these texts. However, the Islamic scholars have argued over whether the prohibition in the Hadith is general, or refers only to the six commodities named.

4.2.3.2.1 *Riba* under Islamic schools

Islamic scholars under different schools disagreed over whether *Riba* is applied only to the six commodities, or it would extend to others which share the same effective causes. The *Zahiri* school refuses to extend the scope of practice on the prohibition of *Riba* to any sources other than those stated in the *Quran* and *Hadith*.³⁵⁵ Thus, this school was opposed to analogical reasoning, and *Riba* was restricted to the commodities that were named in the *Hadith*.

The four primary schools of Islamic jurisprudence brought the prohibition of *Riba* from the secondary sources, although some schools consult addition sources. As a result, there is no difference of opinion among these schools 'that analogically *Riba* [covers] other commodities not mentioned in the *Hadith*'.³⁵⁶ However, 'If there is any difference it is in the analogy used to arrive

³⁵⁰ Ahmad, 'Riba, Its Economic Rationale and Implications'; see MA El-Gamal, *Islamic Finance: Law, Economics, and Practice* (Cambridge University Press 2006) 46–57.

³⁵¹ *Quran* 2:275.

³⁵² Cited in Baamir (n 24) 205; see also Kettell.

³⁵³ Cited in Affi and Affi 203; cited in Baamir 205; see also Chapra 12.

³⁵⁴ Cited in Baamir 204–205.

³⁵⁵ Mohammad Omar Farooq, 'Riba, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?' (2009) 13 *Review of Islamic Economics* 105, 127.

³⁵⁶ Chapra 16.

at the conclusion that the 'addition' [*Riba*] is prohibited for all commodities wherever the analogy holds'.³⁵⁷ Thus, the schools differed in the effective causes for the prohibition of *Riba* as that; in the food, any eaten (*ma'taoum*) food shall be in the rule of *Riba*, and have the same provision of the six above; in the non-food, such as money (*Althmnyah*) shall be in the rule of *Riba*, has the same provision of gold and silver.³⁵⁸ Or any commodity that can be weighed with the exception of gold and silver, shall share in the provision of *Riba*.³⁵⁹

They have not been able to agree on a single opinion because of the distinction between gold and silver on one hand, and the rest of the six varieties on other hand, therefore the effective causes for this prohibition were not identical. The four schools differ in the six commodities in both the value assigned to them and the way that they are traded, and in their relation with regard to *Riba* by using *Qiyas*. Of the six commodities mentioned in the *Hadith*, two (gold and silver) clearly illustrate commodity resources used at that time. Additionally, the differences in the additional sources of *Sharia* law may result in further disagreement on whether the *Hadith* mentions the six commodities as an example, and can be extended to others by analogy. In addition, they may differ as to whether the effective cause derives from one *Hadith* or from more than one. This may result in differences in the interpretation of *Riba* and its divisions and applications.

4.2.3.2 *Riba* types

Riba had been divided by Islamic scholars according to *Quranic* and *Hadith* texts into two types; *Riba Al-Fadl* and *Riba Al-Nasihah*. In Arabic '*Fadl*' means *increasing* or *excess* while '*Nasihah*' means *delay*, *rescheduling* or *defer* for an addition.³⁶⁰ *Al-Nasihah* means extra interest added to the main interest that was caused by *Riba Al-Fadl*, or on an interest-based loan or debt due to the delay in payment. *Riba Al-Nasihah* was widespread and in the *Jahilyah* (the pre-Islamic period) people used to give a money for a stipulated increase, provided that the principal amount of the loan remained intact, and another increase in case of a delay in repayment.³⁶¹

³⁵⁷ Chapra 16.

³⁵⁸ According to the second opinion of Hanbali and the opinion of *Shafi* and *Maliki*, see Ibn Qudama, *Al-Mughni, in Arabic* (3rd edn, The House of Books World 1997) 139–140; Al-Imam Ibn Hajar Al-Haytami, *Tuhfat Al-Muhtaj Bi-Sharh Al-Minhaj, in Arabic*, (Dar Al Kotob Al-Ilmiyyah 2011) 272–278; Al-*Shafi*'i 25; See also Farooq, '*Riba, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?*' 127–130.

³⁵⁹ According to the opinion of Hanafi, and the first and third opinions of Hanbali, however, the first opinion of Hanbali was mixed between first '*Althmnyah*' with regards to gold and silver, and the second '*weight*' with regards to other goods. Ibn Qudama 4/133–138; Al-Imam Ibn Hajar Al-Haytami 4/278; Ibn Alhmmam Hanafi, *Fath Al-Qadeer Fi Sharh Hedaya* (Dar Al Kotob Al-Ilmiyyah 2003) 5/274; see e.g. Farooq, '*Riba, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?*' 127–130.

³⁶⁰ Baamir 205; Chapters 2–5; El-Gamal 50; A Saeed, *Islamic Banking and Interest: A Study of the Prohibition of Riba and Its Contemporary Interpretation* (EJ Brill 1996) 35.

³⁶¹ See Baamir 205; Fakhr-Aldeen Al-Razi, *Al-Tafseer Al-Kabeer* (1st edn, Dar Al-Fikr 1981) 7/85; Farooq, '*Riba, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?*' 106–107.

Additionally, as Al-Shyatibi has observed, the *Riba* prohibited by the text of the *Quran* was only *Riba Al-Nasihah*, but the text of *Hadith* added *Riba Al-Fadl*.³⁶² Al-Tabri noted that Pre-Islamic *Riba* could either be growth at a stipulated maturity date if the principal is not repaid,³⁶³ or consideration for a deferred payment if of a loan.³⁶⁴ There are several other sub-divisions.³⁶⁵ It is not the prohibition of *Riba* that is in dispute by scholars but rather the transactions that constitute *Riba*, but it is agreed that interest associated with loan contracts or debts is *Riba*.³⁶⁶ And ‘that *Riba* among other things includes interest’.³⁶⁷ There are many arguments in this regard in the present between scholars, authors, economists, and legislators due to differences in the effective cause of the six commodities. Where finding the effective cause for the prohibition of *Riba* was limited to single evidence, it caused misunderstanding. Thus, the main reason for the prohibition was not clear for all of them because of the weakness of effective cause.³⁶⁸

This disagreement has resulted in different opinions with regards to *Riba Al-Fadl*³⁶⁹ under different schools. There are those who believe that the only *Riba* is *Riba Al-Nasihah*:

‘There is, thus, absolutely no difference of opinion among all schools of Muslim jurisprudence that *Riba al-nasihah* stands for interest and, is haram or prohibited’.³⁷⁰

Others believe that necessary and simple interest is not *Riba*,³⁷¹ and that the only forbidden *Riba* is that which results in the accumulation of interest and refers to interest redoubled, or to injustice.³⁷² This opinion believes that it must distinguish between productive loans and consumptive loans, borrowing for conspicuous consumption and loan for business purposes.³⁷³ Although there have been attempts to distinguish between interest and *Riba*, these attempts have entirely failed to convince the entrenched:

All attempts to separate interest from *Riba* have supported the interest system which the contemporary Islamic countries came to accept under external forces a century or two ago. Yet these attempts have entirely failed to convince true

³⁶² See Baamir 205; Saeed 32–35; Abu Ishaq Al-Shyatibi, *Al-Muwafaqat Fi Usul Al-Fiqh* (Dar Al-Makrifah) 4/41; Affi and Affi 195–203; Farooq, ‘*Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?’ 106–107.

³⁶³ Mohamed Ibn Gareer AL Tabari, *Jam’ih Al-Biayan* (Dar al Marif) 3/101.

³⁶⁴ Tabari 3/101. Ahamed Ibn Ali Al-Razi, *Ahkam Al Quran* (Dar Tebaht Al Kutub) 1/184; Mohammad Al-Shawkani, *Fath Al-Qadeer* (Daral-Kotub Al-Ilmiyyah 1994) 3/265.

³⁶⁵ *Al-Riba Al Jali* (‘Clear *Riba*’) reflects *Riba Al-Nasihah* and *Al-Riba Al Kaffi* (‘Hidden *Riba*’) reflects *Riba-al-Fadl* (Ibn Al-Qayyim, see e.g. Abdul Azim Islahi, ‘*Economic Thought of Ibn Al-Qayyim (1292–1350)*’ 11–15), and *Riba al-Nasihah* also called *Riba Al-Duyun* (*Riba* on debt), while *Riba Al-Fadl* is also called *Riba Al-Buyu* (*Riba* in trade).

³⁶⁶ El-Gamal 46–57; Jalaluddin Al-Suyuti, *Al-Jami’ Al-Saghir*, p 2/94; Ahmad, ‘*Riba*, Its Economic Rationale and Implications.’

³⁶⁷ Chapter 1; Ahmad, ‘*Riba*, Its Economic Rationale and Implications.’

³⁶⁸ Saeed 32–35; Ahmad, ‘*Riba*, Its Economic Rationale and Implications’; Farooq, ‘*Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?’ 130–133.

³⁶⁹ El-Gamal 51; Farooq, ‘*Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?’

³⁷⁰ Farooq, ‘*Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?’ 107.

³⁷¹ Ahmad, ‘*Riba*, Its Economic Rationale and Implications’; Mohammad Omar Farooq, ‘The *Riba*-Interest Equation and Islam: Reexamination of the Traditional Arguments’ (2009) 6 Finance 99, 109.

³⁷² Farooq, ‘*Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?’ 137; Farooq, ‘The *Riba*-Interest Equation and Islam: Reexamination of the Traditional Arguments’ 111.

³⁷³ See Chapra 3; see also Farooq, ‘The *Riba*-Interest Equation and Islam: Reexamination of the Traditional Arguments’ 111.

Muslims all over the world. Besides, Al-Azhar' Islamic Research Academy in Egypt, The Council of Islamic Ideology (Pakistan), The Islamic *Fiqh* Academy of the Organization of the Islamic Conference, other *Fiqh* academies in the Islamic world have refused and refuted all attempts to justify interest or separate it from Riba.

Where there is a consensus is on the prohibition of *Riba* in all its forms:³⁷⁴

The term *Riba* encompasses interest in all its manifestations irrespective of whether it relates to loans for consumption purposes or for productive purposes, whether the loans are of a personal nature or of a commercial type, whether the borrower is a government, a private individual or a concern, and whether the rate of interest is low or high ... This consensus is clearly reflected in the unanimous verdict of a number of international conferences of fuqaha (jurists) which have been held to discuss the question of Riba, including the Mu'tamar al-*Fiqh* al-Islami held in Paris in 1951 and in Cairo in 1965, and the OIC and Rabitah *Fiqh* Committee meetings held in 1985 and 1986 in Cairo and Makkah respectively.³⁷⁵

Jurists and authors were unsuccessful in finding a consensus, either in terms of the effective cause of *Riba*, or in the interpretation of *Riba Al-Nasihah*. Ahmad has presented some arguments and alternatives but they have not proved convincing enough. He concludes:

Any argument, in this respect, should be viewed therefore as an attempt on our part to understand and explain the 'wisdom' rather than the 'reason' of Riba prohibition. It should be made clear in advance that all arguments concerning the economic rationale of interest prohibition should not on Sharia basis be taken 'reasons' for Riba prohibition. Arguments and theories may be accepted or rejected but Riba will remain prohibited and condemned in Islam. On the whole, therefore, the system which is prohibited by Sharia, is adversely affecting economic development ... the difficulty to understand the prohibition comes from lack of appreciation of the whole complex of Islamic values, and particularly its uncompressing emphasis on socio-economic justice and equitable distribution of income and wealth.³⁷⁶

Furthermore, 'the jurist who resorts to *Qiyas* takes it for granted that the rules of *Sharia* follow certain objectives (*maqasid*) that are in harmony with reason'.³⁷⁷ However, 'the Islamic economic theory is still in its formative stage, dependence is heavily placed on theoretical arguments and hypotheses within the boundary of Islamic rules and ethics'.³⁷⁸ Thus, it is necessary to find the Islamic economic rationale for the prohibition of *Riba*, where 'Interest is not the only form of *Riba*, but it is the most popular one'.³⁷⁹ As a result, *Riba* would be in a form of interest and would be in goods also, unless that it is not every interest would be *Riba*. The result it can differentiate between legitimate compensations and unlawful interest, under *Sharia* law.³⁸⁰

³⁷⁴ Ahmad, 'Riba, Its Economic Rationale and Implications.'

³⁷⁵ Al-Sanhuri, 1953-4, Vol.3, pp.241-2 and al-Qaradawi, 1994, pp. 129-42. The Pakistan Council of Islamic Ideology clearly reflected this consensus when it concluded in its 1980 report on the elimination of interest from the Pakistan economy (Chapter 1); Kutty (n 25), 604.

³⁷⁶ See Ahmad, 'Riba, Its Economic Rationale and Implications.'

³⁷⁷ Farooq, 'Riba, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?' 127.

³⁷⁸ Ahmad, 'Riba, Its Economic Rationale and Implications.'

³⁷⁹ Ahmad, 'Riba, Its Economic Rationale and Implications.'

³⁸⁰ El-Gamal 49.

However, the prohibition under *Sharia* law should take into account, whether is adversely affecting economic development, as it is believed,³⁸¹ or not. Therefore, the jurist must apply the law whenever its effective cause is known to exist regardless of its reason.³⁸²

4.2.3.3 The closest effective cause and meaning of *Riba*

The disagreement between the Islamic scholars in the effective cause '*il'lah*' of *Riba* resulted the differences in the types of *Riba* on one hand and the interest and its applications on other hand. *Riba* is divided into types: *Riba* based debt which includes loans, and *Riba* based-sales. By reviewing all evidence and arguments, it shows that the *Quran* and *Sunna* prohibit indirectly these two types. *Riba* in debt and in goods would be either *Riba Al-Fadl* or *Riba Al-Nasihah*, or together, with little difference. In *Riba* based loans or credit, the increase is interest while the increase in *Riba* based-goods is considered a similar commodity. However, *Riba* is not like trade, where in trade it sells goods for money (in the course of a business), but in *Riba* practice or dealing, it is only money buy-and-sell back for the same product for mere benefit or interest, which is causing a debt cycle.

Returning to the *Quranic* text 'devour not usury, doubled and multiplied' and the *Hadith* text that 'any loan draws a benefit is *Riba*' shows that these texts refer expressly to the prohibition on *Riba*-based loans, whether simple or compound, and the six commodities *Hadith* refers to expressly the prohibition of *Riba*-based goods. However, each of the six commodities in the *Hadith* was used as a medium of exchange at the time when these goods were most prevalent³⁸³ which might suggest that the *Hadith* did not refer to these items exclusively, but as an example, and thus *Riba* is not just limited to these six commodities.

Using the *Qiyas* analogy and reviewing all evidence, there will be an implied effective cause behind, covering all commodities; which is a symmetry (*tamaathol*), whether in sales or loans, if commodities are entirely similar then they shall be equal in number and value to protect the trade circle and economy cycle. Any commutative commodity should be in equilibrium with the same commodity, to keep equality *tamaathol*, and not just in the six commodities. It was observed by Ibn Rushd the 'the prohibition is imposed only for equality in exchanging fungible goods'³⁸⁴ although, Ibn Rushd did not address the main reason and the related effective cause (*il'lah*), where that the reason for the prohibition of *Riba* is to prevent injustice and exploitation, stated by El-Gamal, Chapra and Farooq. This now applies only to sales for money, as bartering has become rare and with it the need to exchange goods.

³⁸¹ Ahmad, '*Riba*, Its Economic Rationale and Implications.

³⁸² *Riba*, Interest and Six Hadiths: Do We Have a Definition or a Conundrum?' 130.

³⁸³ Saeed 32-35.

³⁸⁴ Cited in El-Gamal 53 he commented on the opinion of Ibn Rushd, but his comment was not convincing enough.

Riba-based loans would involve *Riba Al-Fadl*, which is *Riba*-based sales, and would involve *Riba*-based debt, which is *Riba Al-Nasiah* if there is delay. A loan contract is a reciprocal contract which may begin with *Riba Al-Fadl* through the exchange of a similar commodity for future interest, while the increase in the event of delay is *Riba Al-Nasiah*. However, non-loan contracts, even if for money, or contracts where the prices are variable, should be hand-in-hand or like-for-like, or would be either *Riba Al-Fadl* or *Riba Al-Nasiah* or both. *Riba* contract is a contract based on the intention to take advantage of the money in loans, or take advantage of assembling a single product in other contracts, and both lead to economic imbalance. Thus *Riba* be in two types: any interest-based loan, whether it simple or compound, or the increase in the exchange of similar goods.

That interest in commercial transactions may be in loans or in compensation, but not in sales. Therefore, the second type of *Riba* should be excluded due to the lack of *Riba* based goods at the moment, except in limited and rare cases. As a result, interest will be only in loans and compensation, but only the interest-based loan is forbidden under *Sharia* law, and so not all interest is *Riba*; it may be *Riba* if it is just linked to debt in some aspects. *Sharia* law prohibits interest-based loan/debt, which is considered as substantive thereby the violation such substantive is unenforceable under *Sharia* law as mentioned above. Whether simple or compound interest for any period are prohibited.

The concept of usury under *Sharia* law differs from the others in terms of the usury under other concepts linked to interest. Thus, in the Islamic concept of usury, it may be interest or something else, and not all interest is usury, while in other concepts any usury is interest and not all interest is usury, but that interest may be subject to a usury limit. The researchers must look at legal interest rates as being respectable law, without giving consideration to the analysis of economists and their explanations or other effects. Regardless of any reason or under any circumstance, this law has been formulated. *Sharia* law is a law that must be taken into consideration without classification in the event of enforcement of the foreign arbitral awards under the NYC, when the parties have agreed upon it.

4.2.4 *Law and practice of interest in Islamic countries*

The differences among different Islamic schools reflects directly in Islamic countries, either in terms of distinguishing between simple and compound interest in loans, or the distinction between interest and compensation. However, the effect differs in these countries for two reasons: first, the status of *Sharia* law in the Constitution, that is whether *Sharia* is the main source of legislation or just one source; and second, to what extent other laws influence these countries.

The constitutional provisions in Islamic Arab countries may indicate that *Sharia* law is the only source of law, as in Saudi Arabia,³⁸⁵ or the main source, as in Egypt,³⁸⁶ and the UAE.³⁸⁷

In some countries there are civil codes but these codes have been directly influenced by other laws and legal systems to varying degrees.³⁸⁸ European laws are the most prevalent, particularly in an attempt to separate commercial law from *Sharia* law.³⁸⁹ For instance, Egypt clearly adopts the Civil Law system and has been influenced by the Napoleonic Code, but this influence has come through several stages and the current law also reflects strongly the principles of CISG.³⁹⁰

In UAE, the situation is unclear. Its law is strongly influenced by *Sharia* and by a mix of laws including Egyptian and Kuwaiti.³⁹¹ The commercial laws in these countries are the most affected by western laws, while *Sharia* embraces only specific areas such as family law and personal status.³⁹² The most influential legal system in such countries is the Civil Law system, and its impact and connection are clear. Some countries that have adopted *Sharia* law such as Saudi Arabia reject following other legal systems.³⁹³ As a result, in Saudi Arabia the law refers directly to *Sharia* law which covers both civil and commercial matters, and there are no civil codes but there is commercial regulations. However, in Saudi Arabian law there is no mention or prohibition of interest.³⁹⁴ Thus it is unclear whether charging interest in loans, debts, and compensation is permitted or not. Further complications arise with interest-based loans and interest-based debt are prohibited under *Sharia*. To summarise, in all of Islamic countries, there are different interpretations of *Riba* and there is a conflict between the practices and the law of interest or constitution. To clarify this issue, the researcher will examine the law and practice of Saudi Arabia which will be contrasted by the Egyptian and UAE practice in the next part of this chapter.

4.2.4.1 Saudi Arabia

Saudi Arbitration law refers to *Sharia* and dominates and limits the choice of law in three stages if Saudi Arabia is the seat of arbitration or Saudi law is the law governing the arbitration agreement. Under the Saudi Arbitration law, *Sharia* is applied in three places and takes precedent

³⁸⁵ Article 7 of The Basic Law Of Government 1991.

³⁸⁶ Article 2 of 'Constitution of the Arab Republic of Egypt [Egypt] (2014).

³⁸⁷ Article 7 of the UAE Constitution 2011.

³⁸⁸ Kutty (n 25) 595.

³⁸⁹ Akaddaf 20.

³⁹⁰ Akaddaf 20.

³⁹¹ Baamir 218; Kutty (n 25) 595.

³⁹² Akaddaf 20–21.

³⁹³ Baamir 218–220; Kutty (n 25) 595; Akaddaf 20.

³⁹⁴ There is no mention in the Code of Commercial Courts of 1931 issued by Royal Decree No.32, or even the Banking Control Art issued by Royal Decree No. M/5 dated 22/02/1386 H. (1966), and its enforcement regulations do not use the word 'interest' in its text, either in banking codes, financial regulations, the Arbitration Art 2012 or the Enforcement Law 2013.

if *Sharia* is violated at any stage: in enforcement of the arbitral agreement, enforcement of the contract and in enforcement the arbitral award. In addition, *Sharia* is applied in all cases where the arbitral award is asked to be enforced in Saudi Arabia under the Enforcement Law.

4.2.4.1.1 Practice

The prohibition on interest varies in some practical and theoretical aspects according to differences in judicial review of issues either foreign or domestic, and to the difference in judicial decisions under different competent authorities. In practice, it can be divided into: governmental practice; the practice of banks; the provisions of legal committees; cases heard by the courts; and arbitration cases. The Saudi Government itself deals with interest and *Riba* in some of its agreements, and issues securities that are repayable at maturity for a sum above the original sum.³⁹⁵ The Saudi banks charge interest on loans and compensation for delays in payment, although these practices clearly contradict *Sharia* law. Such practices can be seen in SAMA legal actions, where the banking system and bank disputes under the jurisdiction of the Committee Of Banking Settlement of Disputes are under the umbrella of SAMA.³⁹⁶ For example, the Committee issues its provisions in favour of banks, issues punitive provisions including restrictions on banking activities and travel bans, and imposes interest.³⁹⁷ Issues relating to cheques, bonds and securities are discussed by the legal committees in the Saudi Ministry of Commerce including the Commission for the Settlement of Investment Disputes,³⁹⁸ although the decision was over whether the amount claimed by the plaintiff included interest which cannot be enforced, and if the plaintiff only deserved the main sum without interest or compensation.³⁹⁹

With regard to insurance, the Committee to Settle Disputes and Irregularities of Insurance under the Ministry of Finance considers such disputes.⁴⁰⁰ Although this type of contract is forbidden according to *Sharia* law, cooperative insurance has been excluded. Thus, while some

³⁹⁵ Examples in practice: the gas concession agreements concluded in 2004 have a specific clause for interest charged on the sum of the financial guarantee if late payment. However, Article 18 in all three-gas concession agreements provides for interest to be charged for late payment at the rate of LIBOR plus 1%, despite the fact the *Riba* is prohibited under *Sharia* law. See Article 18 of the Concession Agreement, between Saudi Arabia and Lukoil Saudi Arabia Ltd, Umm Alqura Gazette, issue No. 3990 dated 15/03/1425 H. (04/05/2005); Saudi Arabian Monetary Agency v Dresdner Bank AG [2004] EWCA Civ 1074, [2005] 1 Lloyd's Rep 12, where SAMA receives interest on assets deposited or invested from international financial institutions: David E Spiro, *The Hidden Hand of American Hegemony: Petrodollar Recycling and International Markets* (Cornell University Press 1999) 100; A Shoult, *Doing Business with Saudi Arabia* (Blue Ibex Limited 2006) 42, where the Government of Saudi Arabia has been financing its budget deficit through internal borrowing where the major Lenders are the General Organisation of Social Insurance and the Pension and Retirement Fund.

³⁹⁶ See Royal Decree No 8/729 on 10/07/1407 HA.

³⁹⁷ Decision No. 239/1428 dated 23/11/1428 H, 2/12/2007 in case No 104/1428; decision No. 202 /1429 in 4/6/1329 H, 8/6/2008 in case No. 92/1428.

³⁹⁸ According to Royal Decree. No. M/1 on 01/05/1421 AH. Article XXVI of the Implementing Regulations of the foreign investment in Saudi Arabia.

³⁹⁹ Case No. 83 of the year 1405 AH.

⁴⁰⁰ Ministerial decree April 8, 2013.

Islamic scholars believe an insurance contract constitutes *Riba*,⁴⁰¹ the truth may be that insurance contracts do not contain *Riba* but may contain *Gharar* and gambling, a cause of widespread controversy. Insurance may be considered within commercial activities, but the Commission does not explain whether insurance is within civil or commercial law, where it may interfere with the jurisdiction of the Commercial Court.

4.2.4.1.2 Conflicting views in judicial bodies

There were conflicts between such committees and Board of Grievances in terms of allocation of jurisdiction, the question whether such disputes come within the jurisdiction of Board of Grievances or not is frequently asked. However, the Board of Grievances “*Diwan Al-Mazalim*” was the competent authority to consider and review arbitral awards pre the current arbitration law 2012, and it is still the competent authority with respect to commercial and administrative disputes (non-arbitration). The conflict of jurisdiction is a result of desiring *Sharia* courts, in the acquisition of such type of transactions, to be under their jurisdiction, due to the apparent conflict between the principles of *Sharia* and the system of banks, where it is particularly unacceptable under *Sharia* law, as the imposition of interest results in *Riba*, in contrast is the main component motive of the banking system.⁴⁰² Following this, banks face a major legal problem, namely, the refusal of *Sharia* courts to recognize the validity of interest in banking transactions. For example, the Board of Grievances rejected the enforcement of a domestic award on the grounds of banks being parties to the dispute.⁴⁰³ However, this was the result of the clash between the Board of Grievances and the Committee on the Settlement of Banking Disputes with respect to jurisdiction. Although that the enforcement of arbitral awards was subject to the jurisdiction of Board of Grievances under the old Saudi Arbitration law 1983. However, there is no change in Arbitration law 2012 with regards to that the award shall not contrary to *Sharia* law or public policy.

The official position is not clear as the government allows banks to charge interest on the one hand but the jurisdiction conflicts and the legitimacy of the committees of banking disputes and the strength of its provisions was left unresolved, despite the fact that the Board of Grievances stated that the resolutions of the committees of banking disputes were binding on the litigants and

⁴⁰¹ See <http://islamqa.info/en/130761>

⁴⁰² Under Article 1 of the Law Of Procedure Before *Sharia* Courts

⁴⁰³ The request for the enforcement of an arbitrable award in relation to a dispute involving a Saudi company and two national banks was filed but rejected by the Board of Grievances on the grounds that it lacked jurisdiction to hear disputes in which a bank is involved. The Board of Grievances decision No. 50/1418 dated 24/01/1409 H. (1988), decision No. 204/d/TJ/10 in 1426 H in the case of No. 3400/2/s of 1426 H; decision No. 14/d/a/15 in 1429 H in the case of No. 1656/3/s of 1428 H; decision No. 18/d/a/27 in 1429 H in the case of No. 3262/1/s of 1428 H; decision No. 24/d/a/18 in 1429 H in the case of No. 53/4/s of 1429 H; decision No. 126/d/a/15 in 1429 H in the case No. 694/3/s of 1429 H; decision No. 201/d/a/1 in 1429 H in the case of No. 3461/1/s of 1429 H; decision No. 3/d/a/15, 1430 H in Case No. 2119/3/s of 1429 H; decision No. 17/d/a/9 1430 H in Case No. 6296/2/s of 1429 H.

must implement the decisions of the Committee.⁴⁰⁴ However, the same court revoked the decision of the Committee of Banking Disputes and considered it null and void due to lack of jurisdiction.⁴⁰⁵ The public relations manager at SAMA pointed out the judicial nature of such a committee therefore, it is entitled to exercise its jurisdiction over the dispute.⁴⁰⁶ However the Board of Grievances was critical of this view and stated that the committee only has administrative authority, and it is not judicial or with judicial likeness.⁴⁰⁷

However, after years of conflict, the Board of Grievances has lost its jurisdiction on such disputes, and as a result the Saudi government held the final decision on the jurisdiction of the Commission on Dispute Settlement.⁴⁰⁸ *Sharia* courts and the Board of Grievances are not competent for the settlement of disputes relating to banking activities. The separation is clear in law and practice where the Committee of Banking Disputes allows banking interest-based the loan, debts or credit cards and therefore is totally contrary to the Constitution, law and public policy. It is supposed to take into account *Sharia* law because it is the Constitution and internal regulations must not conflict with *Sharia* law. However, the Committee of Banking Disputes takes into account the interests of local banks because it represents the central bank, and thus is both litigant and judge whether this practice is contrary to public policy or *Sharia* law or not.⁴⁰⁹

In banking disputes, if the parties are Saudis, there are limited options to settle the dispute, either by SAMA or by resorting to arbitration, which refuses to enforce an award that contains interest and is considered a violation of *Sharia* law.⁴¹⁰ This conflict may be repeated, that the Committee of Banking Disputes allows interest-based loans, and the *Sharia* courts prevent it. In contrast, the presence of non-Saudis in the arbitration agreement provides more choices for the disputing parties, enabling them to resort to international arbitration anywhere in the world. This is a possible option as long as enforcement of the arbitral award in Saudi Arabia is according to the *Sharia* law. However, a foreign arbitral award would not be enforceable if it contrary to *Sharia* law or public policy. Consequently, there is a gap between law and practice, and a conflict between the *Sharia* law and public policy, as it will be discussed in the later chapters.

⁴⁰⁴ Decision No. 103/d/TJ/1 in 1416 H in the case No. 1464/1/s of 1416 H.

⁴⁰⁵ Decision No. 308/1426 in 30/12/1426 H, 2006.

⁴⁰⁶ According to the Royal Decree No. 729/5 in 07/10/1407 AH, 4/b/110 in 1409 AH, 4/b/21134 in 06/05/1423 AH, 4/b/36405 in 26/07/1424 AH and 59 832/b in 29/12/1425 AH, in addition to the provisions and judicial decisions of the *Sharia* court and the Board of Grievances and the Commission on Dispute Resolution commercial paper have no jurisdiction with respect to banking disputes. See Riyadh newspaper, No. 14062 Date 24/12/2006

⁴⁰⁷ Riyadh newspaper, No. 14817 Date 17/1/2009. Additionally, the administrative courts in the Board of Grievances also stated that there is no Appeals Chamber and there is no right to adjudicate disputes in banking. See Riyadh newspaper, No. 15642 Date 22/4/2011.

⁴⁰⁸ Royal Order No 37441 dated 01/07/2012. Its name was changed to the Committee of Banking Disputes and the establishment of a committee of appellate disputes and violations of banking, and that the Commission's decisions are subject to appeal. This prevents courts from hearing claims about banking.

⁴⁰⁹ Baamir 238.

⁴¹⁰ See the Board of Grievances Decision No. 59/1419 dated 28/10/1419 H. (1999).

According to the banks and SAMA practices, such practices reflect the public policy of Saudi Arabia. In contrast, the practices and the interpretations of courts may reflect another aspect of this public policy. It is unclear whether the award of foreign arbitration when it contains interest will be enforced by the Court of Enforcement under such public policy, or will pursue the Board of Grievance's approach of exclusion of interest. This would be the expected legal action if there were no reference to *Sharia* law in the arbitration law or execution law where it can be made a defence with respect to interest loans under public policy. This shows the extent of jurisdiction, conflict of laws and the ambiguity of public policy.⁴¹¹

The legal force of the Committee has changed, which banking disputes are not subject to the Board of Grievances or any other judicial bodies. Foreign arbitral awards, relating to banking disputes that are carried out in Saudi Arabia are referred to the enforcement judge.⁴¹² The Committee shall consider only the issues of individuals and companies referred to it and that do not fall within the scope of the arbitration. Consequently, the function of Committee does not interfere in the arbitration and thereby it reflects public policy of Saudi Arabia in some aspects. However, the banking and its legal systems in Saudi Arabia are by far in the strangest position. This conflict has created a gap between the *Sharia* and the statutes in the framework of the Saudi legal system in various areas. Saudi banks do not strictly follow *Sharia* principles, as they claim. In short, it is contrary to *Sharia* law and the basic law of government: specifically the regulations of the Regulatory Authority.⁴¹³

It is in the theory and the interpretation of the guidelines, their concept and application that public policy of Saudi Arabia in domestic issues is contrary to its stated position in the Arbitration Act.⁴¹⁴ In practice, with regard to interest, contradictions within Saudi Arabia make it difficult to know the legal rules to be followed in arbitration or judicial decision in Saudi Arabia. In any legal system, a contradiction in public policy poses a significant threat to the arbitration process. However, public policy here cannot be defended against constitutional challenge and the law. This contradiction is between the judiciary, arbitration and legal committees in the Ministry

⁴¹¹ This conflict is not only related to the competent authorities, but is also much larger. The clash on this very specific legal issue, which it is economically and religiously sensitive, represents a greater point of controversy between the two schools of thought within the Saudi authorities or even within society as a whole. Despite the Saudi government issuing new Judiciary Regulations and a new Board of Grievances Regulation (Royal Decree No. M/78 of 1st October 2007), a conservative party that rejects any attempt at reform or development and insists on leaving this vague situation against a larger group that seeks the modernization of the system without prejudice to the established principles and moral values of the society. According to Sheik Muhammad Alissa, the head of Board of Grievances and former Minister of Justice. *Okaz Newspaper*, issue No. 2459 dated 11/03/2008. The Sheik added that some judges even oppose computerizing the archive system in addition to the reform of some existing regulations and procedures.

⁴¹² Arbitral awards issued outside Saudi Arabia are not subject to the jurisdiction of the Committee, additionally, a dispute that contains a foreign element even if it a domestic arbitrable award is subject to the execution judge directly, and is not under the jurisdiction of the Committee.

⁴¹³ Article 7 of The Basic Law Of Government; Article 67 of The Basic Law Of Government.

⁴¹⁴ Art 5 of the Saudi Arbitration Art states.

of Commerce, and SAMA makes it difficult to distinguish between public order, *Sharia* law and the laws of Saudi Arabia in practice.

4.2.4.1.3 *Riba* and public policy

Compared with the grounds for refusal of recognition and enforcement of awards listed in art V of the NYC, Saudi Arabia puts an extra requirement on the NYC 1958; the requirement for compatibility with *Sharia* law, and any decision should not be contrary to the principles of *Sharia* law or public policy although it did not specify these principles nor did it put a constitution based on *Sharia* law or specify its commercial law. This means that the decision to accept or refuse awards is based on the judge's interpretations and there are no set guidelines to follow. The judge leaves the option of choice of the law as he deems appropriate, and the judgements vary from judge to judge, where if the lack of case law and the laws or explicit and clear codes in regards with *Riba*, which the judgement or awards floating in a sea of differences. In cases where there is a conflict between *Sharia* Law and public policy then it is entirely possible that two separate judges may interpret the same case in two different ways – one in favour of *Sharia*' Law and the other in favour of public policy – and come to two separate and different conclusions, with *Riba* cases oscillating between them. However, there is also a contradiction in terms of arbitral awards relating to *Riba*.

4.2.4.1.4 Setting aside

Arbitral awards that entitle one of the parties to perform any unacceptable act under *Sharia*, such as paying interest, will be set aside and the court will not enforce the parts contradicting *Sharia*. Judicial review in Saudi Arabia will lead to an indirect application of *Sharia* law, even if the merits of the dispute is governed by a law other than *Sharia*, when such an award is contrary to *Sharia*.⁴¹⁵ The effect of judicial review would be less than the award under the Enforcement Law 2013, and enforcement proceedings before an enforcement judge, unlike the previous law which had them before the Board of Grievances.⁴¹⁶ However, the new Enforcement Law does not protect parties or foreign awards that are unfamiliar to Saudi law or *Sharia* law concepts.⁴¹⁷

⁴¹⁵ Baamir 200.

⁴¹⁶ Enforcement Law 2013 and the Saudi Arbitration Art 2012.

⁴¹⁷ Nicholas Gould, 'Enforcement in Saudi Arabia and the UAE' (*Fenwick Elliott*, 2014)

<<http://www.fenwickelliott.com/research-insight/newsletters/international-quarterly/enforcement-saudi-arabia-uae>> accessed 10 September 2015.

4.2.4.1.5 Separability theory

It has been established that interest-based loan and debt violates *Sharia*, therefore there is no specified punishment for *Riba*-dealing as the practice in some judicial bodies is to avoid the contradicting part of the contract. The approach is to separate the outlawed part of a foreign arbitral award and implement the rest of the award.⁴¹⁸ As in the case in 2011,⁴¹⁹ where the court overturned a part of an ICC award containing usury which was defined as contrary to public policy and *Sharia* law. An application for the enforcement of an arbitral award made in Bahrain was refused because it required one of the parties to pay interest. The Board allowed the enforcement of only the part that complied with *Sharia* and the losing party was forced to repay only the principal without interest. Which means that *Riba* cannot be enforced.⁴²⁰

4.2.4.1.6 Enforcement of the foreign awards

Foreign awards arbitral awards are enforceable in Saudi Arabia, but there are two fundamental conditions which should be taken into consideration. First, reciprocity – if the foreign party is not a signatory to any international conventions which Saudi Arabia is part of. Second, if the foreign party is a signatory to any international conventions, enforcement of foreign awards would be unless the award goes against *Sharia* law, public policy and morals. The legal rules governing enforcement vary from country to country, according to El- Ahdab who stated that 'there are two important poles of reference: *Sharia* law on the one hand and international conventions on the other'.⁴²¹ In addition, there is a difference under Saudi justice with respect to compensation, either for damage or breach of contract, or the delay in payment or delivery.

The scale of the problem was highlighted in an award where the arbitrator pointed out that 'International arbitration addressed the issue of *Riba* as well. In one case, a Saudi defendant argued that pursuant to the doctrine of *Riba* embodied in Saudi law, a plaintiff was not entitled to interest on any arbitration award. The arbitration tribunal held that the doctrine of *Riba* did not bar all awards of compensation for financial loss due to a party not having had the use of a sum of money to which it would have otherwise been entitled. It is clear that the claimant has in fact suffered financial damage as the result of defendant's breach of contract; the doctrine of *Riba* does not preclude an award for the reasonable compensation of this loss. The Tribunal, however, did not award a commercial rate of interest, but rather based the award on a rate that reflected the incidence of annual inflation over the period at issue'.⁴²²

⁴¹⁸ In a statement to the Prince Bandar bin Salman Al Saud, the former counselor of King Abdullah bin Abdul Aziz and chairman of the arbitrators in Saudi Arabia, in April 2014 in the State of Bahrain, where he said specifically "in the case of usury, the outlawed part will be separated from the arbitration award and implementation of the rest of it," published in Al-Riyadh newspaper on the same date.

⁴¹⁹ No 269/Es/ 4 of 1431II

⁴²⁰ See the Board of Grievances Decision No. 19/28 of 1399 H. (1979).

⁴²¹ Ahdab 19.

⁴²² Final Award No. 7063 (1993) reprinted in 22 Y.B. COM. ARB. 87 (1997), IADR Ref. No. 112. Cited in Akaddaf (n ...) 47

Clearly, recourse to arbitration in Saudi Arabia faces numerous obstacles, including the lack of response by national courts and procedural regulations being both confusing and inadequate, which opens the way for appeals against decisions. This results in an increased arbitration period that is contrary to the purpose of the arbitration mechanism. Saudi courts should only perform a supervisory role in relation to decisions and arbitration as stipulated in the new arbitration system, and not impede the arbitration mechanism. It must follow the procedures set out in the new system without creating obstacles unless such decisions are inconsistent with public order and *Sharia* law. It is also there to clarify substantive regulations regarding *Riba* and compensation, and accept the decisions of arbitration, whether domestic or foreign, unless actually incompatible with *Sharia* law.

4.2.4.2 Egypt

4.2.4.2.1 Constitution and Practice

In Egypt, the practice of banks is like that in Saudi Arabia in some aspects, reflecting the conflict with the Egyptian constitution, but this conflict is partial in terms of the power of *Sharia* law as a source of the Constitution. The only partial conflict is due to the fact the *Sharia* law is one of the main sources of Egyptian law. The statutes of interest are codified in Egyptian law, resulting in less confusion. The practical reality both in bank and commercial transactions reflects modern practice, and legislation also provides for the imposition of interest in some contracts.⁴²³ A case involved the conflict of legal provisions allowing *Riba* and the Constitution under *Sharia* law with regard to interest⁴²⁴ Was filed by Al-Azhar University against the Egyptian President. It stated allowing interest in the event of delay in payment under Article 226 of the Egyptian Civil Code is contrary to Article 11 of the Egyptian Constitution. The Court held that, in spite of the prohibition on interest under *Sharia* law, there is no retroactive effect on the second article of the Egyptian Constitution, that the principles of *Sharia* law do not apply, and that Article 2 of the Egyptian Constitution does not mean that *Sharia* is the law of the country. Rather it means that the legislature is required to respect and implement the principles of *Sharia* in drawing up laws. Thus, Article 2 of all Egyptian Constitution has set a limit on the lawmakers for application of *Sharia* in regard to any future legislation, and Art 226 of the Civil Code, passed before the amendment of Article 2, will not be affected and is enforceable, even if it opposes *Sharia* law.

The decision of the Constitutional Court was described as weak and unconvincing. There were those who believe that the Article 2 of the Constitution and the prohibition of usury had

⁴²³ *Constitution of the Arab Republic of Egypt*, 22 September 1971, available at: <http://www.refworld.org/docid/3ae6b5368.html> [accessed 17 September 2014]

⁴²⁴ Baamir 218–219; Saleh Majid, 'Application Of Islamic Law In The Middle East—Interest And Islamic Banking' [2003] *International Construction Law Review*; see also Akaddaf 51.

become part of public policy and must be applied from the date of modification of the Constitution. The application of the law should be under the supervision of the Constitutional Court to ensure it is not against the Constitution. This conflict will create confusion in determining Egyptian public policy and in determining either the law governing contracts or the applicable law despite the existence of legal provisions governing such practices.

4.2.4.2.2 Interest law

In Egypt, the charging of interest is allowed in commercial and civil matters. In case the party delay in payment, such party should pay 5% interest rate in commercial cases as compensation for this delay.⁴²⁵ Moreover, interest rate also would be determined by to the parties' agreement but does not exceed 7 % interest rate under Art 227 of the Egyptian Civil Law.⁴²⁶ However, charging interest above the legal interest rate is contrary to law/public policy under the Egyptian law.⁴²⁷ If the parties agree to illegal interest rate such rate will be reduced to the 7 % rate.⁴²⁸ In contrast, if the parties do not agreed on an interest rate, the interest rate is 5%.⁴²⁹ However, such rates do not apply to the banking transactions where are exempted from the 7% limit,⁴³⁰ Such rate is due from the date of the Award to the date of actual payment under Art 226, but it may start from its due date rather than the date of the award.⁴³¹ It is procedural matter under the agreement of the parties, the time of the actual damage, or the final award. Charging above

⁴²⁵ Art 226 of the Egyptian civil law

⁴²⁶ Moreover, Art 227 of the Egyptian civil law put limits on the rate of interest that can be charged by the parties, where they can agree on an interest rate if it is less than the maximum rate as stipulated by law. See e.g. Gotanda, 'Awarding Interest in International Arbitration' 48.

⁴²⁷ Shalakany Law Office, 'Interest Rates and Arbitral Awards: Issues of Public Policy' (*International law office*, 2008) <<http://www.internationallawoffice.com/Newsletters/Arbitration-ADR/Egypt/Shalakany-Law-Office/Interest-Rates-and-Arbitral-Awards-Issues-of-Public-Policy>> accessed 25 October 2015 'On December 21 1999 the arbitral tribunal rendered its arbitral award and, among other things, ordered the respondent to reimburse the values of the letters of guarantee, as well as interest calculated at the London interbank offered rate (LIBOR) plus 3% per annum, commencing from April 7 1998 until the date of payment...the Cairo Court of Appeal. On July 30 2001 the Cairo Court of Appeal set aside and annulled the arbitral award on account of its violation of Egyptian public policy. The appeal court stated that ordering the respondent to pay LIBOR interest plus 3% per annum exceeded the maximum interest rate stipulated under Egyptian law and thus constituted a violation of public policy.'

⁴²⁸ Shalakany Law Office 'the Court of Cassation stated that the annulment and setting aside should have been partial and exclusive to those parts of the arbitral award that contravened Egyptian public policy, insofar as it is possible to sever those parts from the remaining parts of the award which are consistent with Egyptian public policy... without affecting the validity of the remaining parts of the arbitral award'. In arbitration award rendered (CRCICA), in CRCICA Arbitration No. 577 of 2008, the arbitrator reduced the interest award of 13% to the 7% allowed under Article 227 of the Egyptian Civil Code.

⁴²⁹ Parties Not Indicated see 'Egypt for Foreign Trade v. R.D. Harbottles (Mercantile), Court of Cassation, Commercial Circuit, 64/2010, 22 January 2008' (2009) 1 *International Journal of Arab Arbitration* pp. 174, 174 '... interest that exceeded its rate and is stipulated in article 227 of the Civil Law related to the Public Order in a way that bans any recognition of the arbitral award ... the award regarding this interest rate of 5% is convenient with article 231 of the Civil Law that allows the creditor to request a complementary compensation that is added to the interests when it is proved that the damage that has exceeded the interest has been intentionally caused by the debtor.'

⁴³⁰ See Shalakany Law Office, 'Interest Rates and Arbitral Awards: Issues of Public Policy' (*International law office*, 2008) <<http://www.internationallawoffice.com/Newsletters/Arbitration-ADR/Egypt/Shalakany-Law-Office/Interest-Rates-and-Arbitral-Awards-Issues-of-Public-Policy>> accessed 25 October 2015.

⁴³¹ See 'Egypt for Foreign Trade v. R.D. Harbottles (Mercantile), Court of Cassation, Commercial Circuit, 64/2010, 22 January 2008' (2009) 1 *International Journal of Arab Arbitration* pp. 174, 177.

the stipulated law is considered violation the mandatory law,⁴³² but the court may allow charging above 7% interest rate under the parties' satisfaction on such rate in some circumstances.⁴³³ In addition, under the Egyptian law that the compound interest is illegal.⁴³⁴ However, The Cairo Court of Appeal of February 26, 2003 no. 23 of the 119th judicial year, held that there is no jurisdiction in case the parties have not agreed to subject the arbitration to the Egyptian Arbitration Law no. 27 of 1994. In *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*,⁴³⁵ the arbitral tribunal ruled a compound interest under the ICSID Convention, as deemed appropriate as the standard of compensation for investment. It seems that such matter is substantive under the Egyptian law in case such law is the applicable law whether to the agreement or contract. While it is procedural issue in case a foreign law governs the dispute. But in constant, the enforcement of the foreign arbitral award may be rejected under the grounds of arbitrability or public policy. The arbitral tribunal in an Egyptian arbitration seat may take into account the Egyptian law with regard to interest rates and periods, however, this measure could result in other legal implications with respect to enforcement.⁴³⁶

4.2.4.3 UAE

4.2.4.3.1 Constitution and practice

Although *Sharia* is the main source of legislation in UAE and usury is also forbidden under the federal law of Civil Transactions.⁴³⁷ The influence of *Sharia* can be seen in many provisions such as the Civil Code of UAE of 1987.⁴³⁸ Nevertheless, due to the various sources interpreting *Sharia* law, the interpretation and application of *Sharia* principles has differed

⁴³² See Shalakany Law Office, 'Interest Rates and Arbitral Awards: Issues of Public Policy' (*International law office*, 2008) <<http://www.internationallawoffice.com/Newsletters/Arbitration-ADR/Egypt/Shalakany-Law-Office/Interest-Rates-and-Arbitral-Awards-Issues-of-Public-Policy>> accessed 25 October 2015.

⁴³³ See Court of Appeal of 5 May 1999 No. 41 of the 114 judicial year (Cairo Court of Appeal, Egypt) "allowing 16% interest when the arbitrator acted as an amiable compositeur". The Court of Appeal mentioned in this Case, that Article 39 (4) of the Arbitration Law provides that: "The Arbitral Panel may, if it has been expressly empowered to act as an "amiable compositeur" by agreement between the two parties to the arbitration, adjudicate the merits of the dispute according to the Rules of Justice and Equity without being bound by the provisions of Law." And the Court of Appeal added that in view of the above there is no contradiction to public order -in this case- if the arbitral panel decides that the interest rate mentioned in its judgment is consistent with the rules of justice and equity, even if this interest rate is over the maximum allowed for by Law, because this judgment is based upon the agreement of the Parties to apply the Rules of Justice and Equity and not the provisions of the Law.

⁴³⁴ See Gotanda, 'Awarding Interest in International Arbitration' 48.

⁴³⁵ ICSID Case No ARB 99/6 in 2012 available at < <http://www.italaw.com/sites/default/files/case-documents/ita0531.pdf>> accessed 25 October 2015.

⁴³⁶ See *EU Joint Venture of Three Companies (Contractor) v. An African Tourism Company (Owner)*, Final Award, CRCICA Case No. 175/2000, 28 December 2008, Arbitral Awards of the Cairo Regional Centre for International Commercial Arbitration IV, (Kluwer Law International 2014) pp. 73 – 183, see also *Malicorp Ltd. (UK) v. The Government of the Arab Republic of Egypt and others*, Final Award, CRCICA Case No. 382/2004, 7 March 2006

⁴³⁷ Article 714 of Federal Law No: 5 of 1985 as amended by Federal law 1 of 1987, does not specifically allow for interest, which states that a provision in a contract that provides for a benefit in excess of the essence of the contract (otherwise than a guarantee of rights of the lender) shall be void but the contract shall remain valid.

⁴³⁸ Article 2 of the Civil Code of UAE of 1987, with respect to the interpretation of the Civil Code of UAE, states: 'the rules and principles of Islamic jurisprudence (Fiqh) shall be relied upon in the understanding, construction and interpretation of these provisions'.

between the judiciary and the civil codes as to whether *Sharia* is the main source of legislation and above all other laws,⁴³⁹ or is a source in the absence of any legislative provisions,⁴⁴⁰ or whether the judiciary shall ‘first apply *Sharia* and other laws in force if conforming to the *Sharia* principles’.⁴⁴¹ It also states that the law is not applicable in the event of conflict of laws with the *Sharia* law or public policy.⁴⁴²

Ironically, the UAE laws expressly allows interest-based loans and debt, which are also expressly prohibited under *Sharia* law. A close look of Article 75 of the Law of the Union Supreme Court of 1973 reveals the legal hierarchy of the Egyptian law. Accordingly, the Supreme Court shall first apply *Sharia* and other laws in force if conforming to *Sharia* principles. It may also apply custom, if such custom does not conflict with the principles of the *Sharia*. Such statutes have caused a conflict between the laws of UAE and *Sharia* law and confusion in their application. In practice, the court’s interpretation holds the key to the issue of *riba*. The Supreme Federal Court in several cases has held that such laws do not conflict with *Sharia*, according to their narrow interpretation, arguing the application of the *Sharia* principle of ‘necessity permits what would be otherwise forbidden’.⁴⁴³ Consequently, regardless of whether *Sharia* law is considered only as a source of law or as the source of law, the Court was able to interpret these laws in line with *Sharia*. Thus, it is clear that prohibited interest under UAE law is only compound interest and interest in civil loans, while simple interest is permissible when necessary.

This interpretation is compatible with interpretations of some contemporary scholars and researchers with regard to *Riba* in *Sharia* law, despite doubts were expressed as mentioned above. The UAE has followed one of the interpretive approaches to justify interest accruals as simple interest and, when necessary, it does not violate *Sharia* law, according to their belief. Consequently, the United Arab Emirates does not believe that such a case is contrary to the Constitution and legislation, which provide for interest where necessary. Clearly, the legal system in UAE is different from others, in that the UAE has a federal system and each emirate has also own law governed by the federal law and the Constitution.

However, such interpretation may conflict with the laws of other countries that adopt *Sharia* law as a principal source of legislation and rely on different interpretations, such as Saudi Arabia. In addition, these interpretations may be in conflict with public policy of the UAE and

⁴³⁹ Majid.

⁴⁴⁰ Article 1 of the Civil Code refers to *Sharia* as the first source of law if lack of any legislative provision; see also Article 5 of the UAE civil law of 1970

⁴⁴¹ Article 75 of the Law of the Union Supreme Court of 1973.

⁴⁴² Article 27 of the Civil Code provides that if conflict of laws no law contrary to *Sharia* can be applied and public policy and morals are applicable.

⁴⁴³ See the decision of UAE Supreme Federal Court-Constitutional Department of 28 June 1981; see Decision dated. 06/09/1983; see also No 245/20 on 7 may 2000.

also may lead to confusion. UAE's public policy rules require that laws must not conflict with the principles of *Sharia* law.⁴⁴⁴

Although the Supreme Court of UAE also believes that the only simple interest is permitted, therefore if the interest rate is above the legal interest rates or is compound interest, it would be contrary to public policy. However, the Court of Cassation once found that a rate of 15% does not constitute a violation of UAE's public policy even though that rate exceeded the rate allowed by the law and that allowable under *Sharia* law, according to their interpretation of *Sharia*.⁴⁴⁵ Thus there is either misinterpretation or public policy subject to the same strictures. Such cases are ambiguous, whether the principles of *Sharia* reflect public policy, or are reflected by this interpretation according to the law, or are not subject to any of these criteria.

4.2.4.3.2 Interest law

In UAE, as mentioned before, interest-based loan in civil contract is unlawful.⁴⁴⁶ However, interest in the commercial loan contract is legal and the interest rate is limited to 12% per annum.⁴⁴⁷ If the creditor did not set the interest rate, the rate of interest will be applied under the current market rates but no more than 12%. Thus, there is a supposition in interest of the creditor to get interest in case is not stipulated by the contract unless the parties have agreed to waive such interest.⁴⁴⁸ Although, that charging interest more than 12% pre annum, is considered usury crime which is subject to UAE Penal Code.⁴⁴⁹ However, in a case, the Court found that the rate of 15% per annum was acceptable where such rate was agreed between the parties in the contract, thereby not is amended. The rate starts from the date of the failure in payment till the full amount is paid, it applies to the time period before the claim or according to the parties' agreement.⁴⁵⁰ Such interest rate shall not exceed the main sum.⁴⁵¹ As mentioned before, UAE law allows only simple interest where the compound interest is unlawful.⁴⁵²

Among member emirates within the UAE, inconsistency dealing with this issue is also noted. For instance, the Dubai' law is in conflict with the law of Abu Dhabi, despite that the Civil

⁴⁴⁴ Article 3 of the Civil Code also stipulates that public policy rules are those, which are not contrary to the basic principles of *Sharia*. Article 27 of the Civil Code provides that if conflict of laws no law contrary to *Sharia* can be applied and public policy and morals are applicable.

⁴⁴⁵ The Court of Cassation in case no. 321 of 1999.

⁴⁴⁶ According to Art 714 of the UAE civil code, such interest is void but that the contract is valid.

⁴⁴⁷ Article 76 and 77 of the commercial law of UAE, 1993.

⁴⁴⁸ Article 88 of the Commercial Code states that where a "debtor is late in settling, he shall be obliged to pay the creditor compensation for the delay the interest specified in Articles 76 and 77, provided no alternative agreement is made."

⁴⁴⁹ Federal Law No 3 of 1987.

⁴⁵⁰ Art 61 of the of Abu Dhabi Procedural Code by Law 3 of 1970; see also Art 62 (3) of Abu Dhabi Procedural Code by Law 3 of 1978. See also Arts 78 and 79 of Federal Law No. (18) Of 1993 Commercial Transactions Law.

⁴⁵¹ Art 62 (4) of Abu Dhabi Procedural Code by Law 3 of 1970.

⁴⁵² See Federal Cassation Decision 30 June 1998 (371/18), also under Art 62 (3) of Abu Dhabi Procedural Code by Law 3 of 1978.

Procedure Code of the Federal Law No 11 of 1992 stated ‘All applicable laws, decrees...concerning civil procedure are hereby repealed with the exception of the provisions on interest in commercial transactions which shall continue to be effective until they are regulated by a law;’⁴⁵³ However, Arts 61 and 62 of the Civil Courts Procedures of Abu Dhabi Law No 3 of 1970 are considerable.⁴⁵⁴ Thus, Abu Dhabi courts apply 9% interest rate to the civil contract and 12% to the commercial contract unless the parties agreed otherwise.⁴⁵⁵ It is considered it is not contrary to federal law where it is based on the constitution.⁴⁵⁶ In addition, such matter is considered a judicial custom in Dubai, where may add 9% interest rate as a delay penalty in civil loan contract unless the parties otherwise agreed.⁴⁵⁷ Thus, the parties are free to agree on applicable interest rate, but such rate is subject to a cap of 12% interest rate, if they failure in the agreement it is subject to 9% implied rate.⁴⁵⁸ The interest rate of 12% is considered substantive issue, but it may be different in civil matters from the commercial matters, while it is procedural issue with regards to the time period. It may be different weather is only interest or interest for damages.

4.2.4.4 The conflicts between Islamic countries

The situation in UAE may look similar to the situation in Saudi Arabia with regards to some practices and the use of *Sharia* law, but Saudi courts are stricter. Likewise, the situations in Egypt and Kuwait are similar to the UAE in some aspects with regards to the practice, laws and their interpretations, but the interpretations of UAE are more realistic. In UAE, the practice it is based on both the law and the Constitution together, according to their interpretations, while the practices in other countries are based either on the law or on the Constitution thereby allowing one to marginalise the other. Therefore, these laws can be relied upon to determine either the law governing the contract or the applicable law, in addition to the rules that affect enforcement.

These differences may cause conflict between these Islamic states when referring to *Sharia* law as a law governing contract. The closest law to *Sharia* would be that of Saudi Arabia. As a result, ‘interest contradicts with the Constitutions of all these countries including the UAE itself,’⁴⁵⁹ and the result is contrary to public policy in such countries. Finally, when choosing *Sharia* law as the law governing contract, this law should not be interpreted in accordance with

⁴⁵³ Article 1 of the Civil Procedure Code of the Federal Law No 11 of 1992.

⁴⁵⁴ Art 62 (3) added to the Abu Dhabi Procedural Code by Law 3 of 1978.

⁴⁵⁵ Art 62 (2) of Abu Dhabi Procedural Code by Law 3 of 1970

⁴⁵⁶ See Federal Cassation Decision (130/19) in 3 March 1998.

⁴⁵⁷ See for e.g. Dubai Court of Cassation decisions 333/2005 and 5/2006

⁴⁵⁸ See Euan Lloyd, ‘What Happens When It All Goes Wrong? Terminating a Construction Contract from a UAE Law Perspective’ (*Al Tamimi & Company*, 2015) <<http://www.tamimi.com/en/magazine/law-update/section-11/may-8/what-happens-when-it-all-goes-wrong-terminating-a-construction-contract-from-a-uac-law-perspective.html#sthash.41P0RSeU.dpuf>> accessed 25 October 2015.

⁴⁵⁹ Baamir 218.

the practices in those countries, but according to the sources of *Sharia* law as a legal system, in narrow circumstances according to the jurisprudence in Saudi Arabia.

Such a difference creates a conflict between these countries, and between them and other countries under different legal systems. This conflict may vary, depending on the clarity and ambiguity of these laws, and the connection between these systems to each other. The level of such conflicts that arise would be more complex internationally and would differ from one state to another. Any conflicts within these states would lead to a failure to apply the law and a failure to identify public policy.

4.3 Principles of Contract and compensations

The principles of freedom of contract, *pacta sunt servanda*, obligation and good faith are agreed by *Sharia*, international commercial law and other positive laws; most of these principles are internationally agreed, whether directly or indirectly. Most are also considered substantive rules in national and international contracts, which gives effect to the enforceability of the arbitral award either negative or positive.

4.3.1 *The principle of pacta sunt servanda*

The second important principle of contracts is the principle of *pacta sunt servanda*⁴⁶⁰ which refers to parties' contractual obligation. It means that the contracting parties must meet the obligations of their contract and such contract is the law of the parties. The principle is one of the sources of international law, and 'state practice over the centuries has recognized the fundamental significance of *pacta sunt servanda* as a principle'.⁴⁶¹ This principle is also recognized in *Sharia* law which is one of oldest and the established principles of the *Sharia*. It is a fundamental principle under *Sharia* that parties must abide by and comply with contractual duties. However, *Sharia* does not differentiate between the contracts whether in form of Conventions, Treaties and any other agreement,⁴⁶² whether between individuals or governments.

4.3.2 *Binding*

This principle is related to the first obligation to obey a contract, assuming the contract is valid. *Sharia* recognizes a contract as a legally valid activity and encourages the parties to any agreement to perform their obligations in accordance with the terms of contract, as the *Quran*

⁴⁶⁰ Latin – 'promises must be kept'. An expression signifying that the agreements and stipulations of the parties to a contract must be observed.

⁴⁶¹ Andrew Solomon, '*Pacta Sunt Servanda*' [2008] the American Society of International Law and the International Judicial Academy; Igor I Lukashuk, 'The Principle *Pacta Sunt Servanda* and the Nature of Obligation under International Law' [1989] American Journal of International Law 513, 513.

⁴⁶² Norman Anderson, 'Law Reform in the Muslim World' xvi.

states: 'You who believe, fulfil any contracts you may make'.⁴⁶³ The non-performance of a contract may contradict with some of the *Quranic* texts.⁴⁶⁴ *Quranic* texts repeatedly refer to obligation of contract in a peremptory language.⁴⁶⁵ The word 'fulfil' in the *Quran* may apply to all contracts signed by parties, except in matters which are considered to be unenforceable or void, such as *Riba*. Fraud, force, or in any other illegal activity will remove the obligation to obey the contract and invalidates the contract under *Sharia* law. All contractual obligations should be performed precisely, unless contrary to *Sharia* provisions, or public policy according to *Sharia* law. Such contractual provisions have also been explained in the *Quran* to include international conventions.⁴⁶⁶ Such principles can be applied in private or commercial law, and can also be applied to many areas of financial and international law.⁴⁶⁷

However, the principle of *pacta sunt servanda* refers to the obligation of contract on parties and judges, which can be breached only for reasons specified by law. This approach is reflected in contemporary legislation in many Islamic countries.⁴⁶⁸ Apart from Islamic countries, the breach of the principles of *pacta sunt servanda* based on the violations of substantive public policy was reviewed under the Swiss Statute on Private International Law. The Swiss court states:

the principle of *pacta sunt servanda* is only violated if an arbitration tribunal refuses to apply a contractual provision that it has determined is binding on the parties, or, conversely, if a tribunal imposes a contractual provision that it has determined is not binding on the parties.⁴⁶⁹

This reflects clearly that this principle can be reviewed considered on the ground of conflicts with other principles such as the principle of good faith or public policy, or that the contract is invalid or cannot be performed because of injustice or violation of the law.

4.3.3 Good Faith

The duty to act in good faith is the essence of Islamic contract law,⁴⁷⁰ *Sharia* considers that the parties hold good intentions from the beginning of the contract, and the original belief in the party is that he has good faith.⁴⁷¹ *Sharia* law recognizes good faith in contracts based on the

⁴⁶³ Baamir 70; Muhammad Tahir Mansuri, *Islamic Law of Contracts and Business Transactions* (New Delhi, Adam Publishers & Distributors 2006) 4.

⁴⁶⁴ *Quran* 5:1. 'O ye who believe! Fulfill (all) obligations'. 'Quran' 17:34. 'Keep your promises. You are accountable for all that you promise'. 'Quran' 16:91. 'Fulfil God's agreement once you have pledged to do so, and do not break any oaths once they have been sworn to. You have set God up as a Surety for yourselves.'

⁴⁶⁵ 'Be faithful to your pledge to God when you enter into a pact' or 'O you who attained to faith! Fulfil your bonds' The 'bonds' (in Arabic 'aqd'; pl. 'uqud') which the Qur'an orders followers to observe and fulfil include all types of contracts whether bilateral, multilateral, or any unilateral obligation to which one binds him or herself.' Akaddaf 25.

⁴⁶⁶ Gamal M Badr, 'Survey of Islamic International Law, A' (1982) 76 Am. Soc'y Int'l L. Proc. 56, 56-59.

⁴⁶⁷ Akaddaf 25.

⁴⁶⁸ For example, Art 89 and 148 of Egyptian Civil Code. See Nudrat Majeed, 'Good Faith and Due Process: Lessons from the Sharia' (2004) 20(1) Arbitration International.

⁴⁶⁹ 'Federal Tribunal Rejects Order Public Challenge. Opines on Pacta Sunt Servanda' <<http://uk.practicallaw.com/0-501-8735?service=arbitration>> accessed 22 September 2015.

⁴⁷⁰ See Kutty (n 25) 610; Akaddaf 31-32.

⁴⁷¹ Akaddaf 32.

Quran,⁴⁷² *Summa* and Islamic scholars, and there is a fundamental rule of *Sharia* law in respect of good faith in contracts, which requires consideration of the contract by looking at intent, faith and meanings rather than by looking at the words and structures. In fact, commentators have highlighted the inherent flexibility of contract law under *Sharia*, which takes into consideration modern transactions and leads to the ability to resolve modern commercial disputes.⁴⁷³ Such principles can be seen in most of laws in Islamic Arab countries,⁴⁷⁴ and other legal systems.⁴⁷⁵ In England the situation is completely different, and you cannot identify whether the principle of good faith is or is not recognized under common law.

In English law, in the commercial contract there is no good faith principle as a general rule. However, there are many arguments in this regards, Leggatt J observe that;

Under English Law a duty of good faith is implied by law as an incident of certain categories of contract, for example contracts of employment and contracts between partners or others whose relationship is characterised as a fiduciary one. I doubt that English law has reached the stage, however, where it is ready to recognise a requirement of good faith as a duty implied by law, even as a default rule, into all commercial contracts. Nevertheless, there seems to me to be no difficulty, following the established methodology of English law for the implications of terms in fact, in implying such a duty in any ordinary commercial contract based on the presumed intention of the parties.⁴⁷⁶

According to Jackson LJ:

‘...there is no general doctrine of ‘good faith’ in English contract law, although a duty of good faith is implied by law as an incident of certain categories of contract [...] If the parties wish to impose such a duty they must do so expressly’.⁴⁷⁷

In contrast there are those who observe that there is ‘nothing new to English law in recognising an implied duty of good faith in the performance of contracts’.⁴⁷⁸

Linking the issue of good faith with usury, in Civil Law, the principle of good faith is important and any contract that contains usury is against the principle of good faith.⁴⁷⁹ This approach also reflects the approach of Islamic and Arab countries such as Egypt where in some

⁴⁷² *Quran* 2:224, 5:8, 5:89 and 17:35.

⁴⁷³ Nudrat Majeed, ‘Good Faith and Due Process: Lessons from the Shari’ah’ (2004) 20 *Arbitration International* 97, 103–104.

⁴⁷⁴ Art 246 UAE Civil Code; Art 148 of the Egyptian civil code; Art 198 of the Kuwaiti Civil Code.

⁴⁷⁵ *Pierce v Emigrant Mortg Co BT - F Supp 2d* (2006) 463 221 [225–227].

⁴⁷⁶ *Yam Seng Pte Limited v International Trade Corporation Limited*, [2013] EWHC 111 (QB) at [120]- [131] per Leggatt J

⁴⁷⁷ *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd*, [2013] EWCACiv 200 per Jackson LJ; See *Berkeley Community Villages Ltd v Pullen* [2007] EWHC 1330 (Ch) at [97] per Morgan J; see also *CPC Group Ltd v Qatari Diar Real Estate Investment Co* [2010] EWHC 1535 (Ch) at [246] per Vos J.

⁴⁷⁸ ‘A New Era for Good Faith in English Contract Law?’ (*Allen & Overy Litigation Review*, 2013)

<<http://www.allenoverly.com/publications/en-gb/Pages/A-new-era-for-good-faith-in-English-contract-law.aspx>> accessed 22 September 2015.

⁴⁷⁹ Udo Reifner and Michael Schröder, *Usury Laws: A Legal and Economic Evaluation of Interest Rate Restrictions in the European Union* (Books on Demand 2012) 45; Omri Ben-Shahar, ‘Fixing Unfair Contracts’ (2011) 63 *Stan. L. Rev* 869; Irene Kull, ‘Principle of Good Faith and Constitutional Values in Contract Law’ (1997) 2 *Notes* 1996, 145.

cases dealing with usury is viewed as contrary to the principle of good faith.⁴⁸⁰ In *Sharia* law, the principle of good faith is related directly to *Riba* contracts, and dealing with such a contract is contrary to this principle. Unlike other contracts, which are related to compensation, it is not necessary for these contracts to be the result of bad faith by the parties, unless the compensation is because of debts or tricks.

4.3.4 Party autonomy

Parties often choose international arbitration as a method to settle their disputes because they want enhanced certainty and predictability of their legal rights.⁴⁸¹ In arbitration the parties seek a stable substantive legal system and procedural framework that is neutral.⁴⁸² This cannot be achieved without gaining some freedom to bypass national jurisdiction, which is usually complex and rigorous. The parties are free to submit their disputes to arbitration and choose the law governing their disputes in their agreement through the arbitration process and the principle of parties' autonomy is agreed by most national arbitration acts and jurisdictions and most of rules of arbitration bodies. In addition, this principle is one of the main substantive rules in international commercial laws such as CISG, ICSID, and other conventions, and one of the main substantive rules in *Sharia* law.⁴⁸³

The freedom is more general than simply the approval of a substantive law that governs the disputed issue. Most jurisdictions recognize the autonomy of parties to choose applicable laws that determine the validity of the arbitration agreement, and substantive rules governing the dispute. The principle of autonomy of the parties is protected in international arbitration agreements because it holds a special status agreed upon by in international treaties and national legal arbitration.⁴⁸⁴ The principle 'gained essentially uniform acceptance in the U.S. courts', in the 20th century⁴⁸⁵ and has been accepted as an important principle in the Hague Conference on Private International Law, albeit with some exceptions and limitations,⁴⁸⁶ particularly with regard to public policy. The NYC 1958, Model Law and most arbitration acts put some bars for the parties' autonomy. Lew observes:

⁴⁸⁰ Gerard Caprio, *Handbook of Key Global Financial Markets, Institutions, and Infrastructure* (Gerard Caprio and Douglas W Arner eds, Elsevier 2013) 252; Peter Temin, *The Roman Market Economy* (Princeton University Press 2012) 170; see also Nael G Bunni, *The FIDIC Forms of Contract* (3rd edn, Wiley-Blackwell 2013).

⁴⁸¹ Born (n 22) 2616.

⁴⁸² Born (n 22) 472–563.

⁴⁸³ In Article (28) (1) of UNCITRAL Model Law; Article (49) (1) of English Arbitration Act 1996; Article 182 (1) of the Swiss Federal Private International Law Act; Article (II)(1) of NYC 1958; Article 6 of the CISG Convention; Article IV (1) and Article VII (1) of the European Convention; Article 42 (1) of the ICSID Convention; Article 35 of the 2010 UNCITRAL Rules; Article 21(1) of the 2012 ICC Rules; Article 15 of OIADA Uniform Act on Arbitration 1999.

⁴⁸⁴ Born (n 22) 472–635.

⁴⁸⁵ Born (n 22) 2678.

⁴⁸⁶ Born (n 22).

Party autonomy in arbitration is quite unlimited. Whatever restrictions different legal systems may place on the right of the parties to choose the law to govern their relations, those limitations can only bind the courts of that legal system.⁴⁸⁷

It would be also different in the event that the dispute arises within the international or domestic field. The international disputes would occur within the field of the international private law and may be subject to international conventions and the result would be a dispute that contains a foreign element would be governed by a foreign law, whether the parties have chosen expressly the law that governs the contract or not in event they have chosen either a foreign seat of arbitration or a foreign law of the arbitration agreement, or fall within the concept of international in a national Arbitration Act. Although arbitration is characterised by the parties' freedom in the choice of law and the rules that govern the contract, it is limited to the national law and the national arbitration act and the judicial intervention would mostly give effect to the domestic disputes.

The autonomy of parties may be limited by restrictions from applicable law, whether the parties choose the law or not, and the choice of foreign law may be limited by public policy according to Art V(2)(b) of the NYC. In addition, it may be limited by non-arbitrability if the choice of law is non-arbitrable under the seat of arbitration or under the law of the place of enforcement under Arts V(1)(a) and V(2)(a) of the NYC and by the non-arbitrability concept if the choice of terms and conditions give effect to the validity of the contract. The autonomy of the parties with respect to this research can be divided into four areas: first, the freedom of contract; second, the freedom of parties to choose the law governing the contract; third, the freedom of parties to choose the law governing the arbitration. The discussions on the first parts will pave the way for the discussion on the final part on the freedom of parties to choose their own conditions and interest rate. The second and the fourth may overlap with the first where the freedom to choose the law governing the contract is the result of the nature of arbitration and comes after contracting where the terms and conditions in the contract are the result of the contractual nature itself. Thus, the freedom of contract is precedent to the freedom of choice of law governing the contract and the freedom to choose the terms and conditions of such a contract.

The freedom of contract is limited by the type and subject of the contract under some jurisdictions,⁴⁸⁸ while the freedom of parties to choose the law governing the contract is limited

⁴⁸⁷ Cited in Born, *International Commercial Arbitration: International and USA Spectscmentary and Materials* 552.; See also Born, *International Commercial Arbitration*; Andrea M Steingruber, *Consent in International Arbitration* (OUP Oxford 2012); Simon Greenberg, Christopher Kee and J Romesh Weeramantry, *International Commercial Arbitration: An Asia-Pacific Perspective* (Cambridge University Press 2010); UNITED NATIONS, 'UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT; The Law Governing the Merits of the Dispute.'; Article V (1) and (2) of NYC 1958; Article (34) (2) (b) (ii) and (36) of Model Law.

⁴⁸⁸ David P Weber, 'Restricting the Freedom of Contract: A Fundamental Prohibition' (2013) 16 Yale Hum. Rts. & Dev. LJ 51.

by public policy, the law and mandatory rules⁴⁸⁹ when applying the choice of law by the seat of arbitration or under arbitration law, and when enforcing the arbitral award under the enforcement place under public policy.⁴⁹⁰ In contrast, the freedom of parties to a referral to arbitration or choice of law governing the arbitration is limited by non-arbitrability, the subject of arbitration and the validity of the arbitration agreement, by the scope of the agreement, and the freedom of the arbitrator.⁴⁹¹ The freedom of parties to choose their own conditions and the rate of interest is limited by the law governing the contract or applicable law, and public policy.

Thus, barriers in the referral to arbitration are a reflection of the limits on the freedom of contract itself. The barriers to freedom of the parties to choose their terms and interest rates in the contract is a reflection of the choice of law to govern the contract and the applicable law on the merits of the dispute, which is the influential in enforcement. One may say it is limited to enforcement, or that the arbitral award cannot be given effect due to it being limited by the law of the enforcement place, which draws such limitation of the freedom.

4.3.4.1 Freedom of contract

One of the important principles in contract law is freedom of contract, which in a valid contract takes place through free consent. The principle means that the parties are free to enter into a legally binding agreement based on mutual agreement and free choice.⁴⁹² It allows parties to provide for the terms and conditions that govern the contract and the parties are free to enter into a contract and choose a law or rules that govern their contract exercising their own free will.⁴⁹³ As the parties are free to create their rights and obligations, they also have the right to settle their disputes, and to choose the applicable rules when doing so.⁴⁹⁴ The choice of law and rules:

‘It is an external reflection of party autonomy in the private law area and that freedom of contract is the result of party autonomy in the contract area’.⁴⁹⁵

Freedom of contract is recognized under all legal systems, national and international laws provided that the contract is not prohibited by law⁴⁹⁶ or is limited by implied terms⁴⁹⁷ so as to

⁴⁸⁹ Benoit Le Bars and Raphaël Kaminsky, *France - International Arbitration 2015* (12th edn, GLG 2015) <<http://www.iclg.co.uk/practice-areas/international-arbitration-/international-arbitration-2015/france>>.

⁴⁹⁰ Art V 2 (b) of The NYC.

⁴⁹¹ Acts II and V (1) of The NYC. 1958.

⁴⁹² ‘Freedom of Contract Law & Legal Definition’ <<http://definitions.uslegal.com/f/freedom-of-contract/>> accessed 2 August 2015; ‘Freedom of Contract’ <<http://www.businessdictionary.com/definition/freedom-of-contract.html>> accessed 2 August 2015.

⁴⁹³ Zhaohua Meng, ‘Party Autonomy, Private Autonomy, and Freedom of Contract’ (2014) 10 *Canadian Social Science* 212, 212 <http://www.esccanada.net/index.php/css/article/download/5155/pdf_171>.

⁴⁹⁴ Meng 212.

⁴⁹⁵ Meng 215.

⁴⁹⁶ In general, the parties cannot contract on criminal cases involving offend to ethics and morals, or which are banned by law. See Richard Stone and James Devenney, *Text, Cases and Materials on Contract Law* (Taylor & Francis 2014) 562–563.

⁴⁹⁷ Bernard Audit, ‘How Do Mandatory Rules of Law Function in International Civil Litigation?’ (2007) 18 *Am. Rev. Int’l Arb.* 37, 37.

protect the social and economic interest of society.⁴⁹⁸ Derogating from the implied terms will leave the contract null and void, and they will be enforced even if the parties to the contract attempt to override or modify them.⁴⁹⁹ Although Muslim scholars have engaged in long debate about the legitimacy of contracts of any sort,⁵⁰⁰ in *Sharia* law freedom of contract is permissible unless there is an explicit prohibition. This is the approach taken by the Saudi courts in the interpretation of contracts and issues of conflict, in which Saudi Arabia has derived its position from the *Hanbali* scholar Ibn Taymiyyah with regards to contract law. However, a contract on a matter that is not allowed by *Sharia* law may give effect to be not subject to arbitration. It can be assumed that the Board of Grievances regards arbitration agreements and their award as illegal because of the nature of the underlying contract if, under *Sharia*, it is a void contract.⁵⁰¹

In commercial matters, in contracts involving interest, whether loan contracts or other contracts related to interest, all laws and legal systems recognize the freedom of contracting on this type of transaction unless contrary to mandatory rules. Usury law is one of the mandatory rules in many countries, in both Civil and Common Laws countries.⁵⁰² Thus, making a contract is permitted provided usury laws are not violated, reflecting the freedom of parties to contract on this type of transaction. The basic principle of *Sharia*, states that in acts of worship, the prohibition is the rule and the authorisation is the exception, but in matters of contracts, the authorisation is the rule and prohibition is the exception.⁵⁰³ However, the freedom of contract with respect to contracts of usury is forbidden under *Sharia* law.⁵⁰⁴

In *Sharia* law, any contract which contains usury is null and void, but there are those who see it otherwise.⁵⁰⁵ The whole contract may be null and void, or be voidable, or only a part of it

⁴⁹⁸ Mohammad Reza Baniassadi, 'Do Mandatory Rules of Public Law Limit Choice of Law in International Commercial Arbitration' (1992) 10 Int'l Tax & Bus. Law. 59, 62.

⁴⁹⁹ Michèle Schmiegelow and Henrik Schmiegelow, *Institutional Competition between Common Law and Civil Law: Theory and Policy* (Springer Berlin Heidelberg 2014) 43.

⁵⁰⁰ See Fakhruddin Al-Zayla'i, *Tubenn Alhakika*, bk 4, 87; Al-kasanaa. Badaa'i AL-Sanai (Dar al-kutub al-ilmiah, Beirut, 2003) ch 8, 3588; Mohummed AL-Shafi, *Alommi* (Darr Almarrfah 1990) bk 3.2.; Sheikh Al-Islam Ibn Taymiyyah, *Al-Qawaid Al-Noorania Al-Faqih* (Dar Ibn Aljosea) bk 265.; Ibn Al-qiyam, *Aalam Al-Moqaan* (Dar al-kutub al-ilmiah 1991) bk 1,384; *Quran* 2:29.

⁵⁰¹ Board of Grievances decision No. 11/D/F/2 of 1417 H. (1997). The legal doctrine of '*ma boniya ala batil fahowa batil*', which can be translated as: 'anything based on something illegal is illegal'.

⁵⁰² 'Mandatory rules are mostly of legislative origin (e.g. usury laws), and it is well known that their number increased in all municipal systems during the last century with the expansion of economic regulation...' see Audit 'Mandatory domestic rules may also emerge from case law, by way of implementation of the general concepts of ordre public or mores.'; 'Civil and commercial codes of civil law countries provide default rules for most of the economically important types of contract (sales, lease...loans etc.) In common law countries, codified default rules are an exception, the most important being the codifying statutes for sale of goods and services (the UK Sales of goods Act and Art 2 of the US uniform Commercial codes (UCC) as well as Art 4 UCC for bank loan and Art 2A UCC for leases).' see Schmiegelow and Schmiegelow 43.

⁵⁰³ Sheikh Al-Islam Ibn Taymiyyah, *The Fatwa Al-Kobara* (Dar al-kutub al-ilmiah 1987) bk 3,326; Ahdab and El-Ahdab 633; Baamir 69; Kutty (n 25) 609-610.

⁵⁰⁴ Islamic contracts and others contracts share some legal theories and objectives. The principle of prohibition in Islamic transactions revolves around three things; *Riba* (injustice) and *gharar* (tricked). El-Gamal 8.

⁵⁰⁵ Md Jalil and Muhammad Khalilur Rahman, 'Islamic Law of Contract Is Getting Momentum' (2010) 1 International Journal of Business and Social Science 175, 175.

may be in violation. Given that usury is unlawful un *Sharia*, a contract which contains such a clause is void or voidable. A valid contract must be legal both in its fundamentals (*Asl*) and ancillary components (*wasf*). A void contract is illegal in both fundamentals and ancillary characteristics. A voidable contract is legal in its fundamentals, but is not legal in its ancillary component. *Riba* is a cause of the contract being voidable according to the *Hanafi* school, but a void contract according to other schools. It draws upon the Quranic verse:

‘But if ye turn back, ye shall have your capital sums: Deal not unjustly, and ye shall not be dealt with unjustly’.⁵⁰⁶

In other contracts that are related to interest, it is permissible to make a contract which is valid and enforceable unless there is fraud or a violation of other rules such as good faith. An Islamic contract must have five elements: buyer, seller, goods, price, and formulation (the offer (*ijab*) and acceptance (*qabul*)). There are conditions of these elements which must be adhered to: the seller should have reached majority age; be of sound mind and able to distinguish; be able to provide the money (i.e. not be bankrupt); have entered into the agreement voluntarily; the goods must be available at the time of the contract, with the exception of the *Salam* and *Istisna* contracts where delivery will be in the future; they must be owned by the seller; who must be able to deliver the goods; and the goods can be known by viewing or description. The seller bears all the expenses of delivery, unless otherwise agreed, and the buyer bears the purchase price. The risk of damage before delivery is borne by seller. These conditions apply to sales contracts such as *Salam*, *Murabaha* and *Istisna*. Other forms of partnership contracts such as *mudaraba* and *musharaka* may have basic elements of their own.

4.3.4.2 Parties’ Freedom in Choosing the Contractual Terms and Conditions

As stated, most legal systems allow the parties to choose their own terms, but in some countries those related to interest rates or such conditions violate mandatory rules are not allowed. In loan contracts, the contract is prohibited under *Sharia* law prohibits the beginning of the contract, or *a fortiori* by the same logic if it has additional conditions such as interest rates.⁵⁰⁷ Under other systems, the freedom of parties to choose their rate on such contracts varies from one state to another.

The freedom of the parties to choose conditions relating to other types of contracts is permitted under all legal systems, with the exception of conditions relating to compensation resulting from the delay in payment of debt, merely to delay, or those that relate to punitive

⁵⁰⁶ *Quran* 2:279.

⁵⁰⁷ ‘According to the principle of freedom of contract, parties to the contract are free to include any term or condition as long as these terms and conditions are not contrary to the mandatory principles of the Islamic law, such as those providing for the payment of interest.’ Baamir 76.

compensation.⁵⁰⁸ In England, this is very strict in some aspects, and some terms may be regarded as unfair under English law if the party attempts to avoid his duty by such terms.⁵⁰⁹ English law imposes its law on contracts, regardless of the chosen law or the terms of the parties if, if the term is unfair.⁵¹⁰ Thus, it is radically different from *Sharia* law, which does not impose any conditions on the parties, but avoids any conditions related to debt. These consider *Sharia* provisions and emphasise that the terms of the contract must not be contrary to *Sharia* law.

In Saudi Arabia the parties are free to enter into any contract as long as it is not forbidden in terms of the conditions and subject, and as long as it is not prohibited under *Sharia* law.⁵¹¹ The parties have the right to choose the law, and the court should consider this right. *Sharia* law takes into the consideration the merit of disputes rather than the law of the contract itself, and that the contract should be valid under implied as well as express terms including the prohibition on interest.⁵¹² As a result, Saudi arbitration law emphasises that the choice must not be inconsistent with the provisions of *Sharia* law and public policy. Article 38(1)(c) of the Saudi Arbitration law says that:

when deciding the dispute, the arbitration tribunal shall take into account the terms of the contract subject of the dispute, prevailing customs and practices applicable to the transaction as well as previous dealings between the two parties.⁵¹³

The parties' clauses can be divided into three categories: '(1) the most reasonable term; (2) a punitive term, strongly unfavourable to the overreaching party; and (3) the minimally tolerable term, which preserves the original term as much as is tolerable'.⁵¹⁴ They can be manifested in an agreement containing usury. In general, interest can be related to the period, either from the date of the breach until judgment, or from the date of the breach until after judgement, or until the date of payment of the full amount. Such interest may be compensation for a delay in payment of the debt resulting from the breach. In this case, freedom of contract is passing through several stages: first ensure freedom of contract of the parties, then review the freedom of parties to choose the conditions, and then enforcement. After these stages such contracts may falter, but it may differ if it is a contract related to substantive rules and other procedural rules.

⁵⁰⁸ Under *Sharia* law and English law, there are many differences with regards to the Freedom of the parties to choose these conditions, and the freedom of the arbitrator in the application of punitive damages or other in the event did not specify the law governing the contract.

⁵⁰⁹ Unfair Contract Terms Act 1977; Ss.5, 6 and 8 of The Unfair Terms in Consumer Contracts Regulations 1999.

⁵¹⁰ Ss.8 and 9 of The Unfair Terms in Consumer Contracts Regulations 1999.

⁵¹¹ Baamir 157.

⁵¹² Kutty (n 25) 609–610.

⁵¹³ Art 38 of the Saudi Arbitration Law 2012

⁵¹⁴ Ben-Shahar.

4.3.4.3 Freedom of parties to choose the applicable law

In arbitration, all legal systems recognize of the freedom of parties to choose the applicable law that governs the contract and the merit of dispute, which is the law of the contract. This freedom reflects clearly the nature of arbitration and the concept of private international law. The choice of law would be directly limited to public policy, law or mandatory rules in arbitration seat,⁵¹⁵ or public policy or the law of the country of enforcement itself. Some arbitration laws and conventions refer directly or indirectly to substantive matters as a ground to enforce the award, thus limiting the freedom of parties to choose the law governing the contract.

Although *Sharia* recognizes the freedom of parties to choose the law governing the dispute, but if the parties chosen law that is contrary to *Sharia* law – for example, which allows interest on loans – *Sharia* law would interfere in this choice of law to become dominant. This can be seen in the Saudi Arbitration Act as mentioned.⁵¹⁶ In relation to freedom of contract, *Sharia* recognizes the principle of autonomy of the parties but restricts its scope in terms of public policy and *Sharia* law. Khamees argues that the biggest difference between *Sharia* law and other laws is that *Sharia* put barriers on the freedom of the parties.⁵¹⁷ He also argues that a Muslim is obliged to apply *Sharia* law in all his or her disputes.⁵¹⁸ This view may apply in respect of the judicial system, where the dispute is subject directly to law, but not in relation to arbitration. The basic rule in *Sharia* is to allow the transaction unless it is led to enforce a prohibition because of a violation of *Sharia* law.

Such barriers are not limited to *Sharia* law or to Saudi Arabia, but may be the most severe in usury issues. For instance, England requires that the choice must not conflict with mandatory rules, and that the English Arbitration Act has a direct impact on the seat of arbitration and the applicable law. In France, the U.S. and the rest of the Arab and Islamic countries require that the chosen law should not breach public policy of the seat, whether international or not. However, there is a clear and explicit distinction between the nature of the judiciary and arbitration where both parties and arbitrators have a degree of freedom. The freedom of parties to contract includes writing their rules and the adoption of other rules, and could be left to the discretion of the arbitrator.⁵¹⁹ The freedom of contracting parties includes making a contract or choosing terms and rules, which is the fundamental principle of contract law. In addition, there is a difference between domestic arbitration and international even under *Sharia* law.

⁵¹⁵ See Bars and Kaminsky..

⁵¹⁶ Art 38 of the Saudi Arbitration Law.

⁵¹⁷ Alkhamees (n 137) 264.

⁵¹⁸ Alkhamees (n 137) 264.

⁵¹⁹ Holtzmann 27.

4.3.4.4 The freedom of agreement to the arbitration

Arbitration clause and the arbitration agreement are fundamental matters in determining the nature of arbitration⁵²⁰ where the arbitrator derives arbitration procedures from such an agreement.⁵²¹ The parties' choice of referral to arbitration under the arbitration rules is very important.⁵²² It is necessary to adopt an arbitration agreement where there is nothing prohibiting parties from referral to arbitration.

The arbitration agreement is a contract like any other, but there are barriers in such a contract which prevent its enforcement, both procedural and substantive. The substantive barriers cover the matter of the dispute, and whether such a matter is subject to arbitration or not. Thus, the consent of both parties is limited to matters that are arbitrable and matters that are not subject to arbitration may be limited (see Chapter Five). The procedural barriers are determined by the validity of this contract and may vary from one law to another.

Consequently, parties' wishes to be subject to arbitration may be limited where there is no explicit agreement or if such agreement is invalid under the chosen law that governs the agreement, or if the arbitrator makes an award beyond the scope of the arbitrable agreement under the agreement (see Chapter Five). It is problematic whether the validity of the arbitration agreement is determined by the seat of arbitration or by the chosen law. In addition, the invalidity of the basic contract may affect the validity of the arbitration agreement whether it is connected or separate. There are many views on this issue, but as far as the agreement exists, it may lead to different treatments concerning the arbitration agreement and the law governing the contract's validity. Determining the validity of the arbitration agreement is based on the applicable law, as discussed in later sections.

In general, by using analogy, the rules of contract would contribute to develop the arbitration agreement under *Sharia* law. *Sharia* law does not differentiate between contracts, whether international or domestic, or between individuals or companies.⁵²³ Concepts of the enforcement of foreign and domestic arbitral awards under *Sharia* law largely coincide with the NYC⁵²⁴ and *Sharia* does not differentiate between nationalities or regions, and may be considered to apply more broadly. Referral to arbitration in any form whether internally or internationally does not conflict with *Sharia* law. As a result, there is no obstacle which precludes acceptance of such a type of contract.

⁵²⁰ Berg, 'ICCA Congress Series, 1998 Paris' 118.

⁵²¹ Poudret and others.

⁵²² Koch 325.

⁵²³ Kutty (n 25) 624.

⁵²⁴ Almutawa and Maniruzzaman.

However, some countries, such as Saudi Arabia, are trying to dominate and control the arbitration process by intervening in the law governing the contract. The judicial review of the law governing the contract may be more severe due to the fact that some contracts are prohibited, and the choice of law may lead to them being allowed. Unlike arbitration, where the referral is not prohibited and the freedom of parties to choose the law governing the arbitration agreement is not prohibited, the arbitration agreements or clauses are permissible even if the merit of dispute at the case is not allowed.

Saudi arbitration law intervenes in determining the validity of the arbitration agreement, which could conflict with the NYC under which the seat of arbitration determines the validity.⁵²⁵ Thus, there are three laws which may play in the international arbitration,⁵²⁶ in addition to four laws/countries would give effect to the award: the country of the law chosen to govern the contract, the country that the arbitral award is made, the country of the effective arbitration agreement law, and the country of enforcement. However, regardless of the law chosen by the parties, a contract is binding under all systems, whether a contract or an agreement, if the contract and conditions are legally valid. It is binding on the parties, on the forum court and arbitration tribunal under the law governing the contract. Therefore, without a good reason, national courts have no right to intervene or to impose more conditions on the foreign parties or their chosen clauses to the contract itself, where the contract is subject to a foreign law chosen.

4.3.5 *Arbitration under the autonomy of parties*

Laws may have a negative impact on the applicable law such as Saudi Arabia law, which give adverse effect to the applicable law through the seat of arbitration or the arbitration law, must be amended. Thus, exclusion articles which require that applicable law and the parties' terms shall not be contrary to *Sharia* law. As a consequence, such articles intervene in the applicable law despite the fact that the arbitral award may be enforced elsewhere. However, it is necessary to keep the right of states to refuse foreign arbitral awards according to the considerations grounds of refusal, whether mandatory rules or public policy or the law of the place of enforcement.

Recognition and enforcement in arbitration are in three stages: recognition and enforcement of the arbitration agreement; recognition and enforcement of the contract under the law governing the dispute; and recognition and enforcement of the foreign arbitral award. The application of mandatory rules in arbitration is different from their application before the national court. Arbitration differs from other international laws and conventions that fall within the public international law or the private international law such as CISG convention and WTO. Disputes in

⁵²⁵ See Art II (3) of the NYC and Art 50 of the Saudi Arbitration Law 2012.

⁵²⁶ Born (n 22) 2618 the footnote No 13..

international commercial law with the exception of arbitration, are subject to law but it is considered before the appropriate court.⁵²⁷

In domestic disputes, the dispute and the contract are subject to the law of the court because the contract is not subject to any other law. In contrast, in disputes of the international arbitration, the contract is enforceable by the arbitrator based on the applicable law, and the court shall only consider the foreign arbitral award to ensure: first, at the request of the parties, that the law applicable to the contract have been applied properly; and second, that such a foreign arbitral award is based on the applicable law and does not conflict with public policy, law or mandatory rules. The parties' choice of law replaces both peremptory norms and mandatory rules of the law that would be applied by national court.⁵²⁸

This matter would be different in the event that the dispute is brought before a national court 'judicially' or referred to arbitration. Thus, the dispute coming before the national court would be subject to the national law as a law that governs the dispute. As a result, it is subject to the law and the power of the state, which the parties cannot legislate.⁵²⁹ In arbitration, the parties may expressly choose the applicable law, or may fail to choose the law that governs interest-based loan or interest in other contracts. In addition, they can choose their own terms and conditions with regards to the interest such as higher rates, fixed prices, the payment period or compensation. If they fail to choose the law, the applicable law to the contract would be either be the law of the seat of arbitration, the law of the arbitration agreement, and the most closest and real connection under the conflict of laws rules. As a result, the chosen law, whether explicit or implicit, would determine the legality of such terms, which depends on the following:

- 1- Does the chosen law contain restrictions to freedom of contract?
- 2- Does the chosen law allow these clauses in the contract?
- 3- Are there restrictions to the ability of the parties to pay the interest?

To what extent the arbitrator should follow either party autonomy in such terms or the applicable law, and whether the arbitrator has the authority to consider the dispute under the terms of parties or must follow the law that govern the contract and disputes is also important, as is whether the arbitrator is obliged to consider the three points above in applying the law. As a result,

⁵²⁷ 'With regard to disputes arising from international commercial contracts, national courts usually apply their conflict-of-laws rules in order to define the applicable law...The CISG is a *lex specialis* of the international sale of goods.' See Dawwas and Shandi.

⁵²⁸ Jan Klabbers and Touko Piiparinen, *Normative Pluralism and International Law: Exploring Global Governance* (Cambridge University Press 2013) n 218–226; see also Audit.

⁵²⁹ See Meng: 'In fact, any law (positive law) is linked with the operation of public power (state power). From such point of view, any law is "public" and individual cannot legislate.'

the arbitral award may be set-aside or suspended under the law that has chosen by parties according to Art V(1)(c) of NYC.

In some cases, a contract that contains special terms and conditions may be considered as invalid. In such circumstances, the dispute may be considered non-arbitrable according to Art II and V of the NYC. Thus, there are three laws which may play a pivotal role with regards to contracts which contain interest, whether interest-based loan contracts or other interest-based contracts, which would give effect directly or indirectly to non-enforcement of the award of interest: the chosen law; the law of the arbitration seat that may govern the legality of terms of the parties; or the law of the place of the enforcement.

The matter may also be non-arbitrable if such disputes cannot be settled by arbitration either under the law of the seat of arbitration or the place of the enforcement, or if such terms give effect to the validity of the arbitration agreement. In addition, the award may be set-aside or suspended if the arbitrator fails in the applicable law, or would be considered outside the scope of the arbitration if the parties fail in choice of law and their terms, when the dispute was considered by authority of the arbitrator himself. Such matters may cause that the awarding of interest is non-enforceable if the award under the chosen law is contrary to public policy under the place of enforcement, even if there are no additional terms. These issues will be explored in more detail in later Chapters.

4.4 Compensation and interest in Contract

In commercial contracts a breach of contract comes in several forms, such as a delay in the delivery of goods, the delay in payment, and non-compliance with any of the terms. In sale contracts, the purpose is to deliver the goods and receive the fee, so non-compliance with this exchange is a breach of the sale contract. In addition, under commercial loan contracts the sum shall be paid back to the owner whether with interest or without under different laws as mentioned above. However, the parties are free to agree on any clause unless such clause is unenforceable under the law of the contract under different interpretations. Thus, the parties could agree directly to a clause or indirectly by referral to the law, where some laws apply terms of interest implicitly in case the parties do not do so. In contrast, such a clause may be applied for actual damages or expected damages. Most contracts share the same meaning of a breach of contract, e.g. a breach of contract in construction contracts⁵³⁰ includes delay in project, delay in payment or that any of

⁵³⁰ In construction delay disputes, more common in the commercial arbitration arena, a breach of contract or wrongful act results in the delay, rather than abandonment, of a construction project. Neal Mizrahi, 'The Arbitration Review of The Americas 2012: Compensation in Complex Construction Disputes' (*Published by Global Arbitration review in association with fTi consulting inc*, 2012) <<http://www.fticonsulting.com/~media/Files/us-files/insights/articles/compensation-in-complex-construction-disputes.pdf>> accessed 2 November 2015.

the agreed terms and conditions of a contract is broken. Hence, a breach of contract would be a result of the negligence or breach of duty.

Construction contracts fall mostly within administrative and investments contracts.⁵³¹ However, these contracts may also relate to loans⁵³² and debts through late payment. The most common points between these contracts are non-performance of something essential in the contract, violation of the penalty clause agreed upon, the existence of actual damages albeit without an agreement or damages result by the delay. Breaches can arise from delay in delivery of goods, delay of the project, late payment on a loan, delay of a project related to loan contract, and late payment as a result of a sale contract. Such damages may cost a large amount, whether caused by lost profits as a result of the project delays⁵³³ or by late payment. Some countries require that the remedy shall be reasonable but not punitive and some require that the remedy should be equal to the actual damages. As a consequence, these contracts vary from one legal system to another.

In arbitration, international arbitrators have failed to adopt unified approach to assessing interest claims⁵³⁴ where they are complex. Equal compensation for damages regularly challenges arbitrators and experts.⁵³⁵ Hence, one of the biggest obstacles in the international commercial arbitration is the absence of uniform laws in this regard despite the existence of the CISG Convention,⁵³⁶ Principles of European Contract Law,⁵³⁷ and transnational law principles,⁵³⁸ which refer to interest in case late payment and remedies in case damages and breach of contract. However, matters of conflict in interest laws and interest rates have not been mentioned either in the CISG convention or in transnational conventions, which do not give solutions or uniform these laws. In addition, neither PECL nor *lex trans* principles were able to unify the laws in EU countries where there are still substantial differences between European countries with regards to such matters. Thus, neither Civil Law nor Common Law countries were able to unite laws with each other with respect to damages and interest.⁵³⁹ Although the U.S. has adopted the provisions

⁵³¹ 'Although the nature of claims tends to differ, similar compensation measures are applied in commercial arbitration and investor- state construction disputes.' Mizrahi.

⁵³² 'Generally, with construction financing, interest or principal is not payable until the project is completed and security is based on the title to the underlying property. Once the project is completed, permanent financing, generally based on the market value of the completed project at the time of the loan, is deployed to repay the principal and accrued interest associated with the construction loan.' Mizrahi.

⁵³³ The arbitration panel awarded Sands over \$14.5 million in damages, 24 times the contract fee. Even though the project was only delayed by about four months. See *Permi Corp. v. Greate Bay Hotel & Casino, Inc.*, 610 A.2d 364, 129 N.J. 479 (1992).

⁵³⁴ Gotanda, 'Awarding Interest in International Arbitration'; Hunter and others.

⁵³⁵ Mizrahi 4.

⁵³⁶ Articles 74 and 78 of The United Nations Conventions on Contracts for the International Sale of Goods, (1980)

⁵³⁷ Article 9:501, 9:508, 9:509 and 17:101 of Principles of European Contract Law - PECL

⁵³⁸ See e.g. VII.6 - Duty to pay interest, VII.7 - Right to charge compound interest, and XI.1 - Compensation for expropriation, available at <<http://www.trans-lex.org>> 20 October 2015.

⁵³⁹ Hunter and others.

of CISG and established Uniform Commercial Code (UCC), neither CISG nor UCC refer to interest rates or periods with regards to late payment issues, but give remedies for breaches of contract and other damages.

Such differences and conflicts are not limited only to such countries, but also extend to the entire world, where they can be found in *Sharia* law and within Islamic countries. It is possible that such differences occur even within a single country that has several trends and systems, as is the case in the U.S. However, there is no express reference to awarding interest in the rules of UNCITRAL and the ICC Arbitration,⁵⁴⁰ but some arbitration rules such as LCIA, WIPO and AAA refer to awarding interest, whether simple or compound.⁵⁴¹ In international arbitration, the arbitral tribunals/arbitrators face three issues: the responsibilities of the debtor/party to pay interest, the time period, and the rate of such interest.⁵⁴² In addition, they also must determine whether the parties agree on their terms, whether such terms are acceptable and reasonable under the applicable law assuming the presence of the choice of law agreement, and whether such type of disputes is substantive or procedural matter. Such matters are considered substantive in one country and in another procedural⁵⁴³ depends on whether interest-based loan/debt or compensation is involved.

4.4.1 *Sharia law*

In this section, the discussion is focused on compensation relating to loans and late payments resulting from actual damages or penalty clauses. Interest in the form of compensation may be referred to on the ground that it is not an interest-based loan or debt, such as compensation for delay in payment. Moreover, contemporary Islamic jurists have agreed to prevent the requirement of compensation for the delay the payment, in the form of a pre-arranged percentage or a fixed amount that has already been agreed on. This is because that is the pre-Islam form of *Riba*, which is forbidden under *Sharia* law.⁵⁴⁴ In bankruptcy, Quranic text recommends the

⁵⁴⁰ Natasha Affolder, 'Awarding Compound Interest in International Arbitration' (2001) 12 American Review of International Arbitration 45, 51.

⁵⁴¹ See Art 60 (b) of WIPO Rules; Art 28(4) of the AAA Rules; and Art 26.6 of LCIA Rules.

⁵⁴² See e.g. Gotanda, 'Awarding Interest in International Arbitration' 41.

⁵⁴³ See e.g. Gotanda, 'Awarding Interest in International Arbitration' 52 'Many countries regard the awarding of interest as substantive, 114 while others deem rules concerning interest as procedural. And, in some countries, certain aspects of the awarding of interest are viewed as substantive, and others as procedural.'

⁵⁴⁴ The compensation for the delay in paying off the debt is absolutely forbidden, as in the previous stated, which it is the same as the pre-Islamic *Riba* which was prohibited by the Quran and hadith, whereby the creditor used to ask the debtor in case of delay: either to pay or increase. In the fact of, this practice is applied in many banks around the world and which is approved by many banking regulations even some of Islamic banks, and also the international trade law being based on that. However, that *Riba* is forbidden under the Islamic contracts law and the *Sharia* law, and therefore this methodology will create more disputes between parties, and create more conflicts in laws, due to increasing the interest or compounding it illegally, and which will result to doubling the capital and cause a harm to the debtor.

creditor to give a longer time limit to the debtor.⁵⁴⁵ This methodology is used in Saudi courts and other legal regimes.⁵⁴⁶ Most laws stipulate the legality of compensation against the delay in the fulfilment of debt. This reasoning has been cause for debate among contemporary Islamic scholars.⁵⁴⁷ However, compensation that may be gained for loss of a benefit or an actual damage is permissible as a result of procrastination and such damage.

Without agreeing upon compensation for delay in payment, such compensation pays for the actual damages. The penalty clause, which is named "*shart-jazai*" in Islamic jurisprudence, is related to the contract of the goods and investment for damages and compensations. *Sharia* law prevents the penalty clause in contracts where the original obligation may be a debt because it is outright *Riba*. The penalty clause is considered one of the sensitive matters under *Sharia* law, especially when it is related to *Riba* according to the way of interpretation of compensation and damages. However, it is not necessary that such clause is prohibited under *Sharia* law in all cases where it recognizes the principle of *pacta sunt servanda* and considers the contractors shall fulfil their obligation as mentioned. Compensation for damage is significant in *Sharia* law in commercial matters and other transactions. In addition, it recognizes the right of compensation for torts and crimes.⁵⁴⁸ Such compensations can be found in sources of *Sharia*.⁵⁴⁹ *Sharia* law

⁵⁴⁵ "And if he (the debtor) is poor, he must be given respite till he is well-off. However, if the debtor has delayed the payment despite his ability to pay, he may be subjected to different punishment", see Quran: 2:280. Thus, is balanced by the Quranic verse that obliges the debtor to repay debts, which making it a sin and not just a legal obligation that to pay off all of debts if the debtor has the ability to repay:⁵⁴⁵ "O you who believe, you shall fulfil your covenants". See *Quran* 5:1.

⁵⁴⁶ Saudi Arabia holds the same view according to *Sharia* principles and the view of the general presidency of scholarly Research and *Ifta'* in Saudi Arabia. The regulations of the bankruptcy avoidance and the law of commercial court govern the creditor's rights, bankruptcy and insolvency. There is an asymptotic approach in some of the Gulf Cooperation Council (GCC), and in the international trade law according to Art 58 of Legislative Guide on Insolvency Law of UNCITRAL 2005. See Fatwa No 3700, Part No. 19; Page No. 201. The Bankruptcy Avoidance Regulations promulgated under Royal Decree No. M/16, dated 4/9/1416 H. (24 January 1996); The Commercial Court Law promulgated by Royal Decree No. 32, dated 15/1/1350 H. (1 June 1931).

⁵⁴⁷ Scholars agreed that it is not permissible to compel an insolvent debtor to pay interest or compensation for delay in payment under the teachings of the *Quran*. According to the council of Senior Scholars in Saudi Arabia, Sheikh Mustafa Al-zarka, observes that: The entitlement of compensation is conditional on the debtor in case he has no legitimate excuse in the delay in payment, where he is able to pay but procrastinator. In this instance he deserves to describe him as unjust and as a usurper, see About the admissibility of compel the debtor "procrastinator", to compensate the creditor, *Journal of Islamic economic studies*. C: 2, V: 3, (p. 20), see also: comments of Zaki Chaban on it (p. 198), *Journal of King Abdul Aziz* (p. 20). Moreover, Sheikh Abdullah ibn Mniea: the fine or compensation cannot be applied unless three conditions are available: proof of the procrastination; evidence of ability to repay; and the lack of guarantee payment to the creditor as a full guarantee or warranty, from the Sheikh's Fatwas and Researches (3/239). Etc.

⁵⁴⁸ Tort refers to civil matters, which may include commercial transactions and banking, while crimes are the violations of certain public primary rights, which affect property, the human body, reputation, religion, the state, public peace and tranquility, decency or morals.

⁵⁴⁹ The line which divides the two types of violations – torts and crimes – is sometimes very narrow or, as the Islamic jurists put it, there are some matters in which the rights of the public and the rights of individuals are combined. In tort cases the remedy is usually awarded to the individual, whilst in crimes the remedy is subject to the sovereignty and interest of the state in most aspects. *Sharia* law recognizes compensations for crimes, which namely *diyah* "retaliation". Thus, in cases of infringement of a person's right to personal safety, the Offender pays this compensation or *diyah* to the nearest relatives of the victim or to the victim himself, if he is still alive. However, restitution and compensation are the remedies provided for violation of a person's proprietary rights and for other violations have the same reason. The *Quran* shows *diyah* as an example in the following verse see *Quran*: 2:178. "O you who have attained faith! Just retribution is ordained for you in the case of killing: the free for the free, and the slave for the slave, and the woman for the woman. And if something of his guilt is remitted to a guilty by his brother,

considers the Islamic rules such as '*no harm nor harming*' and 'the harm should be removed' to maintain money and rights, thereby such harm cannot be accepted under *Sharia* law. Rules also say to not award the injured party more than the injury-suffered equal in the provision with the Islamic rule of the harm cannot remove by a similar harm.

Islamic Fiqh Academy stated that a penalty clause for delay in delivery forward of sale is *Riba*.⁵⁵⁰ However, it is a procedural clause, where the parties are free to agree on this clause for this kind of contract, and there is nothing that would make such a clause prohibited. This is through the application of the principle of good faith on the intent of contractual parties, and other principles and rules of the law of Islamic contracts as well as some of the evidence mentioned in the legitimacy of the contracts. Thus, such type of contract is not related to *Riba* but some scholars attempt to avoid it under the Islamic rule of warding off evil taking precedence over bringing benefits.⁵⁵¹ In the event that the contract including such a clause has ended for any reason(s), the buyer may get his money back plus compensation for the delay in delivery of the goods as stipulated in the contract on the grounds of the nature of the contract and the lack of parties' intention circumvent *Riba*.

Conversely, the Islamic Fiqh Academy agreed upon the penalty clause for delay in delivery goods in a similar contract,⁵⁵² although not for the main branch of contract.⁵⁵³ In addition, according to *pacta sunt servanda* the parties shall fulfil their obligation in the case that parties agreed as mentioned above. Thus, the penalty clause is allowed in contract of sale under the rules of *Sharia* under the logic previously discussed. If the parties do not agree on any compensation, a party may receive compensation in event of actual damage under the rules of no harm nor harming, etc. Such compensation would start from the date of delay under the clause or the date of the damage under the general principles and rules of *Sharia* law.

this remission shall be adhered to with fairness and restitution to his fellowman shall be made in a goodly manner". However, compensation for torts can be found through the acts of the Prophet Muhammad, when he changed a pot with a new one after it had broken, and said, "Food instead of food, and pot instead of pot or a vase". Moreover, using the Qiyas in all commercial matters, and important Islamic rules in this area, such as base do no harm as Prophet Muhammad said, "...no harm nor reciprocating harm"

⁵⁵⁰ In the case of "Salam" issued the International Islamic Fiqh Academy in the ninth conference in Abu Dhabi in Article 7 of the resolution "the penalty clause is not allowed for delays in delivery of the goods in Salam contract, because it is a debt, not allowed to get an increase in debt in the case of delay". See the decision No. 85 (9/2) in 1-6/4 1995 of International Islamic Fiqh Academy.

⁵⁵¹ See e.g. A Hourani, *Arabic Thought in the Liberal Age 1798-1939* (Cambridge University Press 1962) 233.

⁵⁵² The Islamic Fiqh Academy itself issued another resolution, five years after, confirms the earlier decision and distinguishes between contract of Salam and contract of *Istisna*. However, the penalty clause is permitted in *Istisna* contract and prevents in the Salam contract, contract of *Istisna*. Although that the *Istisna* contract is part of the contract of Salam and derived from it. See the decision No. 109(12/3) in 23-28/9/2000 of International Islamic Fiqh Academy.

⁵⁵³ Sale of *Salam* contract (forward of sale) giving the money in advance and delay the receiving of goods. Another type of sale contract is divided from the first one, as for created for manufactured goods (*Istisna*) where the contract calls for goods to be manufactured, in the same meaning. They may be called future sales of goods or services.

4.4.1.1 Late payment

Islamic scholars have differed in their opinions on the matter of compensation for damages due to delay in payment. The first opinion emphasizes that the debtor is not bound to pay compensation for the creditor for losing profits resulting from the late payment of the debt, regardless of whether it is a clause inserted into the original contract or not.⁵⁵⁴ This is in an attempt to avoid charging interest in the form of *Riba* in these circumstances. The second opinion emphasizes that it is permissible to compel the procrastinating debtor who is capable of fulfilling the debt to pay compensation even if it is not provided in the contract. Such compensation is paid to the creditor for losing a profit as a result of the delay.⁵⁵⁵ However, they may differ as to whether

⁵⁵⁴ This opinion was stated by decisions of jurisprudential academies and Islamic scientific bodies, which includes the majority of contemporary scholars. Among those who agreed on it from the Contemporary Islamic scholars and wrote in this opinion: Prof. Dr. Ahmed Fahmi Abu Sna, in the magazine Al-Azhar (p. 754), C (7), year (63) Rajab 1411 AH, Dr. Nazih Kamal Hammad, supporters to carry the legitimacy of the debtor "procrastinator" to fulfil (p. 295), Dr. Ali Salous, in the journal Almjma, No 6 (1/264), Dr. Takiia Ottoman, in contemporary doctrinal issues (p. 40), Dr. Mohammed Shabir, as in the fourth seminar of Kuwait Finance House (p. 281), Dr. Hassan Alomeyen, in commenting on the search Zarqa (p. 41) in the Journal of Islamic economic studies (v: 3, p: 2), Dr. Rvieq Almusrra as in the Journal of the compound, No. VI (1/334), Sheikh Abdullah bin Beah as in commenting on the search Zarqa (p. 54) in the Journal of Islamic economic studies (v: 3 - p: 2), Dr. Zaki Din Shaaban also in commenting on the search Zarqa p. 99, in the Journal of King Abdul Aziz University in 1409 AH, Dr. Mohamed Zaki 'Abd al-Barr also commented on Al-Dharier opinion (p. 61), in the Journal of King Abdul Aziz University in 1411 AH. In accordance with decision of the Islamic Fiqh Council of the Muslim World League, in session 11, in 1409 H - 1989, stated: " if the creditor required the debtor or imposed on him to pay him a sum of money, in form of a fine penal specific or a certain percentage in case of delaying payment according to an agreement between them, then this condition would be void, and should not be fulfilled, which is not permissible, whether that condition from a bank or other; because this particular is Riba of Jahilyah (pre-Islamic period of ignorance) that is prohibited by Quran". See Resolutions of the Islamic Fiqh Academy of the Muslim World League, 268. Available at <<http://en.themwl.org/2012/05/19/resolutions-of-the-islamic-fiqh-council-11th-session-1409h>> 20 October 2015. Furthermore, a resolution of the Islamic Fiqh Academy of the Organization of the Islamic Conference at its sixth session on the sale of instalments as reads follows:

"Third: If buyer delay in the payment of premiums for the deadline, it is not permissible to make him pay any increase in the debt, even with the conditions precedent or unconditionally; because it is Riba which is forbidden. Fourth: It is not permissible for the debtor who is proven "able to pay" to procrastinate in the performance of the instalment. However, it is not permissible in *Sharia* law to require compensation in the case of late performance "See Majalah Al Majma, NO 6, (1 / 447-448). Moreover, according to the standard of the procrastinator debtor, which adopted by the Accounting and Auditing Organization for Islamic Financial Institutions -AAOIFI, as follows: "(b) It is not permissible to stipulate a compensation, whether compensation for loss of profits (missed opportunity), or a change in the value of the currency. (c) It is not permissible to claim jurisdiction of the procrastinator debtor to let him pay compensation in cash or in kind for the delay payment or debt". See Accounting, Auditing & Governance Standards (for Islamic Financial Institutions), English version, 2010, p 34. Available at <<http://www.aoofi.com/aoofi/Publications/KeyPublications/tabid/88/language/en-US/Default.aspx#account>> 20 October 2015. It is also prevented by the Supervisory Board of Cooperative Development Bank Islamic Sudan dated 06/08/1406 H. See Ahmed bin Ali Abdullah, proposed actions to address procrastination, p 6. In Arabic

⁵⁵⁵ Among those who agreed on it from the Contemporary Muslim scholars and wrote in this opinion: Sheikh Abdullah bin Suleiman bin Mniea, in his Fatwas and Research (3/191-266), Dr. Mohamed Zuhayli, in an unpublished paper entitled: compensation for the damage from the debtor procrastinator, pp. 81 - 82, submitted to the Accounting and Auditing Organization for Islamic Financial Institutions in Bahrain 1421. Dr. Abdul Hamid Baali, the basics of Islamic banking (p. 57-59) and Sheikh Mohamed Khater, the proposed actions to address procrastination (p. 5); and Mustafa bin Ahmed Al Zarqa in his article: about the permissibility of the compulsion of debtor "procrastinator" to compensate the creditor, published in the Journal of Economic Studies doctrinal, p 20, e: 3 Edition: 2, Year 1417 H. "The principle of compensating a creditor for damage, as a result of procrastination by the debtor and a delay in paying off the debt in a timely manner is acceptable in Islamic law, and nothing in the provisions of Islamic law and its origins, and purposes of the public is incompatible with it. On the contrary, they support this view and regard it as obligatory, and the entitlement to such compensation is imposed on the debtor, as the debtor does not have a legitimate excuse to delay. As such he deserves the description as unjust as usurper". Moreover, Sheikh Abdullah Ibn Mniea states that: "The view that says: should compensate for what the creditor lost from his money due to the procrastination, is totally the view of which supported by Sharia rules and assets, and the clear and explicit texts in the Quran and Hadiths". See Sheikh Abdullah bin Suleiman bin Mniea, in his Fatwas and Research (3/193).

this amount is in the loan contract or sales contract, or as debt resulting from the delay in payment. Moreover, whether there was an actual damage or merely a clause in the form of a penalty clause.

In loan contracts, if the parties agree on such compensation or interest, it will not be permissible according to the first opinion by the arguments previously stated. In case of actual damage, compensation is allowed for such damage in accordance with the second opinion and according to the rules described above. In non-loan contracts, if the parties have stipulated such compensation shall be permissible, if it is not then it shall be equal to the actual damage. This dispute does not arise with regard to direct sales contracts, which give money for goods without delay in any of them. However, it may also vary according to the type of these contracts, where most differences are in futures sales. In the case of futures sales and when the money is delayed, the penalty clause may be allowed for delay in payment provided simple interest was applied and there is no interest on the debt resulting from such delay. For several reasons, the contract is a contract of sale where the exchange of different items, according to the freedom of the parties and in accordance with the principle of good faith, that the interest is not the sole intent of the contract, but rather to adjust such a transaction. Indeed, interest-based debt is *Riba* under *Sharia* law, but in reality the debt would not be only after the date of late payment and thus the interest as a penalty would start from the date of the payment that the parties agreed upon, not from the date of contract. Additionally, these contracts are valid under the justice and logic in the application of the penalty clause on all parties in accordance with the interests of both of them under their agreement. Both parties also deserve compensation for actual damage. In the case that goods are deferred, then it is not the case that the money also would be deferred due to it being selling debt by debt, which is invalid according to *Sharia* law.⁵⁵⁶

4.4.2 Saudi Arabia

The real confusion is found in compensation for commercial contracts, especially compensation related to delays in the project or payments, and in penalty clauses. In some cases where the claimant is Saudi Arabian, the judgement may go in favour of that party as has been seen on several occasions, which sometimes calls into doubt the impartiality of the Saudi judiciary.⁵⁵⁷ Confusion may occur because of the lack of reliance on the basis of the law or *Sharia* itself and the lack of judicial precedent. In addition, judicial review affects the enforcement a

⁵⁵⁶ If the seller has not received the full price in the contract time it will be sold of a debt against a debt, where the Islamic scholars have argued that such transaction is called 'ba'i Al dayn' is prohibited according to four grounds. It would be *Riba*, *gharar*, the lack of possession by the buyer, and the risks that face the buyer and seller due to debts. See Muhammad Yusuf Saleem, *Islamic Commercial Law* (John Wiley & Sons Inc 2013) 21; see Mohammed Obaidullah, 'Financial Options in Islamic Contracts: Potential Tools for Risk Management' (1999) 11 J.KAU: see also *Islamic Econ* 2–26; Muhammed Hashim Kamali, 'Islamic Commercial Law: An Analysis of Futures' (1996) 13 *The American Journal of Islamic Social Sciences* 211–212.

⁵⁵⁷ As in the case of Emaar Properties PJSC based in Dubai and Jadawel International, a Saudi company.

foreign award. Judicial rulings with regards to interest vary in terms of theoretical and practical, and in practice it depends on the competent authority that will consider it, rather than being based on fixed codes, a fixed base, or judicial precedent, though it should at least be based on *Sharia*. However, it is difficult to determine the legal actions of Saudi courts in compensation settlements due to a scarcity of cases and lack of transparency. In the enforcement of foreign arbitral awards, the enforcement judge in all cases considers interest-based loans or debt, or compensation. It is unclear to what extent the judge would give effect to the enforcement of foreign arbitral awards with no judicial review and on what basis the decision would be made. It is particularly confusing for foreign arbitrators and judges on loans contracts and compensation or damage.⁵⁵⁸ The issue is further complicated by the confusion between interest rates and whether it constitutes a matter of substance, bankruptcy and compensation issues, which have relevance with usury in some respects.

Decisions do not depend on the opinions of legality in Saudi *Sharia* bodies or jurisprudential academics, nor do they rely on judicial precedents. Thus, provisions often contradict themselves due to the religious opinion of the judge with regards to '*Furu al Fiqh*', which may also conflict with the opinion of other Islamic scholars. It can be argued that this process is deliberate and encouraged as the judges are allowed to impose their own interpretations on the provisions associated with each case. However, all Saudi judges agree on the '*Usul al Fiqh*', which includes the prohibition of *Riba* and that the judge can use the methodology of *Ijtihad*. Arbitrators in arbitration applying *Sharia* law to the contract and disputes can also use *Ijtihad*. Through the freedom of the parties, and the rules and principles of *Sharia* law, each case can be considered separately.

However, compensation for actual damage is legal, even for harm or delayed delivery of the project or goods, but it is void for other transactions and delayed payments under *Sharia* and Saudi law.⁵⁵⁹ Compensation for delayed payments, if it is due only to the delay itself, it may be

⁵⁵⁸ See Award No. 7063 (1993) (Saudi Arabia v. Saudi Arabia), 22 Y.B. COM. ARB. 87, 89 (Int'l Comm. Arb. 1997) (describing an arbitration proceeding in which the defendant argued that the claimant could not recover an award in addition to substantive damages according to Saudi Arabian law and the doctrine of *riba*); cf. Jason Chuah, 'Islamic Principles Governing International Trade Financing Instruments-A Study of the *Morabaha* in English Law' (2006) 27 *Northwestern Journal of International Law and Business* 137, 27. (recounting a case in which a defendant argued that an English court should invalidate a contract because it is illegal under Saudi Arabian law). (Concluding that an additional award of damages was not prohibited because the *Sharia* prohibition against interest is subject to a number of exceptions under modern Saudi commercial practice); (confirming that the arbitral tribunal in the Award no. 7063 of 1993 refused to apply the *riba* doctrine's ban on interest to all arbitral awards of compensation for financial loss).

⁵⁵⁹ See Case No. 545/1 / s for the year 1419 HA, the first Judgment No. 109 / d / a / 4 in 1426 HA; Case No. 141 / T / 1 for the year 1427 HA, Date of the Judgment 20/2/1427 AH brought before the Board of Grievances, Administrative Court. Conclude; do not deserve compensation for elongation of the implementation period, as they are the cause of this delay. Do not deserve compensation for all acts of conservation and protection, for being one of the appropriate contract and order as long as it has done before the receipt. As for the delay in the disbursement of entitlements, the company cannot compensate for damage unless it proves it, which shows that the court rejected the compensation for being not proved the actual damage.

interpreted as *Riba*, as it is interest-based debt.⁵⁶⁰ Generally, if the actual damage has been proven by evidence, this will remove the confusion and therefore the compensation will be legal. If the compensation is for delayed payment, the compensation will be unfair if the delay was caused by a good reason and was not due to the negligence of the party that caused the delay. In the case of negligence and actual damage, the claimant may get compensation but it must be equal to the actual damage.

4.4.3 *English law*

In England, there are several laws in relation to compensation for the delay in payment or delivery of the goods, a breach of contract or damages in general. In construction projects, the party may have a right to claim interest in construction disputes or other types of disputes related to interest such as claims for loss and expense, delay and disruption, and defects. In addition, the party is entitled to demand interest and compensation in credit contracts, and the supply and sale of goods contracts etc. However, such right is considered also by the English Arbitration Act under the parties' agreement to the terms of the contract or as an implied term under the governing law such as Late Payment of Commercial Debts (Interest) Act 1998, Consumer Credit Act 1974, Unfair Contract Terms Act 1977 (the UCTA), The Unfair Terms in Consumer Contracts Regulations 1999 (the UTCCR) and Sale of Goods Act 1979.

The Late Payment of Commercial Debts (Interest) Act 1998 applies a minimum interest of at least 8% a year on the price of goods or services as an implied term in commercial contracts, plus a fixed sum and reasonable costs of recovering the debt.⁵⁶¹ Such, 'implies a term into such contracts that such debts are to carry statutory interest in the same way as interest carried under an express contractual term'⁵⁶²The start date of the interest is determined under the parties' agreement, under the arbitrators' power, or under the applicable law to the contract i.e. the Late Payment Act.⁵⁶³ However, the Late Payment Act does not apply to damages or to post-award interest and is only for simple interest. English law considers liability to pay interest to be a substantive issue and the period and rate of interest to be procedural issues.⁵⁶⁴ However, paying

⁵⁶⁰ There are many of banking transactions deal with compensation as a penalty for the delay. Case No. 1079/1 / s for the year 1425 HA, the first Judgment No. 69 / d / a / 10 in 1426 HA, Audit rule No. 94 / T / 1 for the year 1427 HA, Date of the Judgment 01/2/1427 AH brought before the Board of Grievances, Administrative Court. The court rejected the lawsuit, because of the lack of proof for the damage, and due to it also includes interest for delay on bonds, and Sharia law forbids it. Thus, the judge refused to compensate because of the suspicion of *Riba* in bonds.

⁵⁶¹ See 'Guidelines for Arbitrators on How to Approach the Making of Awards on Interest' (*Chartered Institute of Arbitrators*, 2011) <<https://www.ciarb.org/docs/default-source/practice-guidelines-protocols-and-rules/international-arbitration-guidelines-2011/2011awardsinterest.pdf?sfvrsn=4>> accessed 9 October 2015.

⁵⁶² *Martrade Shipping & Transport GmbH v United Enterprises Corporation [2014] EWHC 1884 (Comm)* [11].

⁵⁶³ See s 4 of the Late Payment of Commercial Debts (Interest) Act 1998

⁵⁶⁴ See Craig C Martin and Jason J Green, *International Arbitration and Litigation* (Jenner & Block 2014) 44; See Gotanda 52 'In England, for example, liability to pay interest is considered substantive, but the period for which interest accrues and the rate of interest are deemed procedural'; Triebel 12 'Since interest payable on an English judgment debt is treated as a procedural matter, governed by English law'.

interest is substantive under the English law in case such law has been chosen by the parties. If not, then it is procedural under the English Arbitration Act under international arbitration. Furthermore, the Arbitration Act gives the arbitrators the absolute freedom to consider any interest over period, which means even below 8% or at no interest, especially if it is governed by a foreign law due to there being no mandatory rate of interest.⁵⁶⁵

The interest rate is not intended to be compensatory. It exceeds the rate at which most commercial creditors would be likely to have to borrow whilst being kept out of their money. It can properly be regarded as a penal rate which is intended to act as a deterrent so as to promote the purposes of the Act reflected in section 6. Two purposes are identified. One is the need to protect commercial suppliers whose financial position makes them particularly vulnerable if their debts are paid late. The other is the general deterrence of late payment of commercial debts. The application of the rate is not limited to commercial debtors or creditors of a particular size or kind. It is not discretionary, save to the extent that the conduct of the parties may justify its disapplication in whole or in part (section 5). The Act is intended to promote prompt payment of all commercial debts and discourage the use of delay in payment as a business tool for commercial advantage, not only in order to protect the vulnerable but also as a matter of general policy. The Act gives effect to domestic socio- economic policy and seeks to promote the benefit of prompt payment of debts on the economic life of the United Kingdom.⁵⁶⁶

The Late Payment Act provides remedies for the debt resulting from late payment for supply of services and sale of goods contracts or any debt created by an obligation under a contract.⁵⁶⁷ However, this Act gives effect only if the contract falls under the provision of the Act, such remedy is for debt and not damage, and the obligation of the payment is in the whole or part of the contract price.⁵⁶⁸ In addition, the Act would be only applied if it has been chosen by the parties.⁵⁶⁹ The parties in contracts may exclude the right to interest under such Act, but only if they provide a substantial remedy for late payment. Such remedy must be fair and reasonable to compensate, and sufficient enough to prevent late payment. If the remedy is too high, it is considered to be punitive, unfair or unreasonable, and therefore unenforceable.⁵⁷⁰ However, UCTA and UTCCR require the terms of contract shall be reasonable or the implied terms would be applied in some circumstances. As a result, the Late Payment Act would be applied implicitly under the legislation. If the remedy is too low, the Late Payment Act may not apply automatically,

⁵⁶⁵ See e.g. Joe Tirado/ Winston & Strawn LLP, 'England & Wales - International Arbitration' (*global legal insights*, 2015 6 'No mandatory or customary rate of interest is applicable'; see also Gotanda 44 'Interest is customarily awarded under the Act whenever a claimant has been deprived of the use of money or assets, unless the parties have expressly agreed otherwise.'

⁵⁶⁶ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWIIC 1884 (Comm) [12].

⁵⁶⁷ See s5, s6, s7, s8 & s9 of the Late Payment of Commercial Debts (Interest) Act 1998.

⁵⁶⁸ Section 3 (1) of the Late Payment Act

⁵⁶⁹ 'A debt does not carry statutory interest if or to the extent that it consists of a sum to which a right to interest or to charge interest applies by virtue of any enactment (other than section 1 of this Act). This subsection does not prevent a sum from carrying statutory interest by reason of the fact that a court, arbitrator or arbiter would, apart from this Act, have power to award interest on it. ...A debt does not carry (and shall be treated as never having carried) statutory interest if or to the extent that a right to demand interest on it, which exists by virtue of any rule of law, is exercised.' See section 3 of the Late Payment of Commercial Debts (Interest) Act 1998.

⁵⁷⁰ See s 8 and 9 of the Late Payment of Commercial Debts (Interest) Act 1998.

but excluding the right to statutory interest in this regard would cause the contract clause to be void.⁵⁷¹ This Act considers the freedom of the parties with regards to the contract terms 'which deal with the consequences of late payment of the debt'.⁵⁷² Hence, this freedom includes the waiver of interest and reliance on guarantees as an alternative to these consequences.

4.4.3.1 Unreasonable terms

Indeed, unreasonable or unjust terms lead to court intervention into the parties' terms of contract and their freedom with regards to the debt incurred by late payment, thereby it may be limited to the Late Payment Act. Under s12 of the English Arbitration Act where such provision is mandatory, this allows the court to intervene in case the contract terms are unjust.⁵⁷³ In addition, under the s4 of the English Arbitration Act, the mandatory provisions will be applied regardless of the law applicable to the agreement, which means s12 will be applied in case of injustice. Although s12 does not specify contract terms that are considered unjust, in the case of interest, the Late Payment Act may be applied which provides 8% interest rate. This may cause conflict with freedom of the parties and the power of the arbitrators to award any interest rates for any period, and others remedies under the English Arbitration Act.⁵⁷⁴

Although the jurisdiction of the arbitral tribunal in the English Arbitration Act applies to substantive issues, unless the parties otherwise agreed,⁵⁷⁵ the arbitrator's award under the arbitration agreement applies as the same force and effect of the court judgments.⁵⁷⁶ In addition, objection to the jurisdiction of the arbitral tribunal can be made if the substantive issues are considered outside its jurisdiction.⁵⁷⁷ Thus, under unjust terms under the English law, the court may intervene in the recognition and enforcement of award, where it will be set aside or unenforceable under the English Arbitration Act s13.⁵⁷⁸ The English Arbitration Act is comprehensive and well-outlined, stating where mandatory provisions govern in case the disputes included unjust terms,⁵⁷⁹ when the arbitral award will be set aside,⁵⁸⁰ when the arbitrator may be

⁵⁷¹ See s 8 of the Late Payment of Commercial Debts (Interest) Act 1998.

⁵⁷² See s 8 (5) of the Late Payment of Commercial Debts (Interest) Act 1998.

⁵⁷³ As a result, "the court shall make an order only if satisfied [that] one party makes it unjust to hold the other party to the strict terms of the provision in question" ... "and any other enactment (whenever passed) relating to the limitation of actions", thus that the M1 Limitation Act 1980, the M2 Foreign Limitation Periods Act 1984, and may other Acts such Late Payment 1998 etc. See s12 (3) (b) of the Arbitration Act, 1996, such Art is considered mandatory.

⁵⁷⁴ S48 and s49 of the Arbitration Act, 1996

⁵⁷⁵ S30 of the Arbitration Act, 1996

⁵⁷⁶ S66 (1) of the Arbitration Act, 1996

⁵⁷⁷ S31 (2) of the Arbitration Act, 1996

⁵⁷⁸ See s13 of the Arbitration Act, 1996, such Art is considered also mandatory. 'in respect of a dispute which was the subject matter of an award which the court orders to be set aside or declares to be of no effect, or of the affected part of an award which the court orders to be set aside in part, or declares to be in part of no effect...'. In addition, under Art V (1) (e) of NYC, or under non-arbitrability and the public policy under Art V (2) of NYC.

⁵⁷⁹ S12 of the Arbitration Act, 1996

⁵⁸⁰ S13 of the Arbitration Act, 1996

removed,⁵⁸¹ and where there are objections to the jurisdiction of the arbitral tribunal.⁵⁸² The arbitral tribunal handles unreasonable or unjust terms under the Late Payment Act etc. in the event that the parties have chosen the Late Payment Act as a law applicable to the contract, or under the Arbitration Act s12 when the parties have chosen the English Arbitration Act as the law applicable to the arbitration agreement. The arbitral tribunal considers the parties' terms, the chosen law, and s12 of the Arbitration Act if the unfair terms have the same legal effect of the Late Payment Act.

However, with regards to the unfair terms under the Act 1996, in a case,⁵⁸³ the English Commercial Court intervened in the jurisdiction of the arbitral tribunal despite the Claim Submissions was uncertain. This court held that the tribunal adopted a "half-way house" approach due to the partial award. However, failure to give the parties an opportunity to have their dispute considered may cause a serious irregularity and a substantial injustice. The court 'therefore found that the parties should have been given opportunity to address the tribunal's proposed course of action'. The court sent the dispute back to the tribunal to determine whether the failure caused substantial injustice to the party, which for these reasons the tribunal might have reached a different result. Although s30 provides the arbitrators may rule on their own substantive jurisdiction on matters that have been submitted to arbitration under the arbitration agreement, unless otherwise agreed by the parties⁵⁸⁴ the objection can be made against jurisdiction of the arbitrators if they are exceeding their substantive jurisdiction, but it is limited to some specific reasons⁵⁸⁵ and if there a good reason why the matter should be decided by the court then it will be heard.⁵⁸⁶ It seems such action is a procedural matter, where the court may intervene in case the action will result in injustice without considering the agreement of the parties with respect to the interest rate, but it may be considered under the agreement or under the arbitrator's power.

In *Yuanda (UK) Co Ltd v WW Gear Construction Ltd*,⁵⁸⁷ the claimant argued that the clause is void or invalid under section 3 (1) of the UCTA 1977, due to there being amendments included that changed the interest rate for late payment from 5% to 0.5%, a rate also void under the Late Payment Act 1998. The claimant also argued that the clause was not fair and reasonable.

⁵⁸¹ S24 of the Arbitration Act, 1996

⁵⁸² S31 of the Arbitration Act, 1996

⁵⁸³ See e.g. Craig Tevendale and Hannah Ambrose, 'Lorand Shipping v Davof Trading (Africa) B.V. (MV "Ocean Glory"): When a "creative Solution" on the Part of the Tribunal Becomes a Serious Irregularity Leading to Substantial Injustice' (*Herbert Smith Freehills*, 2014) <<http://hsfnotes.com/arbitration/2014/11/04/lorand-shipping-v-davof-trading-africa-b-v-mv-ocean-glory-when-a-creative-solution-on-the-part-of-the-tribunal-becomes-a-serious-irregularity-leading-to-substantial-injustice/>> accessed 28 October 2015.

⁵⁸⁴ See s30 (c) of the Arbitration Act, 1996.

⁵⁸⁵ See s31 of the Arbitration Act, 1996.

⁵⁸⁶ See s32 of the Arbitration Act, 1996.

⁵⁸⁷ [2010] EWHC 720 (TCC)

it was not insufficient, and not a substantive remedy and thereby the statutory interest rate should be applied under the Late Payment Act 1998.

However, Mr Justice Edwards-Stuart held that, 'it seems to me that the imposition of the statutory rate is the penalty that a contracting party pays for failing to provide in its contracts a fair remedy for late payment to suppliers'.⁵⁸⁸

He observes that in case of any lower rate of interest provided in the contract, the Late Payment Act only substitutes the statutory rate if the contractual rate does not afford a substantial remedy. He commented that there is no reason why 5% could not be substantial remedy; even 3% and 4% interest rates above the base would be substantive remedy. The interest rate of 0.5% was not substantial remedy because they did not discuss individually, thereby there is no reason why it be fair and reasonable.

Although, the term 'reasonable' can be found in both Late Payment and Unfair Terms Act, there is no clear meaning of the concept under these laws. UCTA refers indirectly to bad faith and fraud, especially in section 3, although it does not provide explicit definitions. Such meanings can be found in the comments of Justice Edwards-Stuart, where he referred to the intent and the negotiation of the parties. He would recognize the interest rate 0.5% if it were individually discussed, as he observed that even interest rates of 3% and 4% above the base are substantive remedy. Likewise, the Late Payment Act, where the word 'oust' and the phrase 'imposed by one party to the detriment of the other' in the meaning of the substantial remedy, indirectly refer to bad faith.⁵⁸⁹ Additionally, with the misinterpretation of the terms of the contract and 'strength of the bargaining',⁵⁹⁰ it can be said it is referring negotiation under the bad faith. Thus, the above provisions under the concept of non-reasonable and unfair do not directly relate to the interest rates, but in the procedures related thereto. There is no clear determination of the substantial remedy, but the statutory interest rate is alternative to the rate of the contract terms if there is any evidence of bad faith etc., otherwise under the freedom of contract it would be determined under the valid agreement and proper negotiation of the parties.

4.4.3.2 Applicable law

Under the Arbitration Act the parties and the arbitrators have absolute freedom in determining remedies and interest rates, while the Late Payment Act and others may limit that freedom. There is a conflict between the two laws, thereby when the choice of law limits the authority of the parties and the arbitrators, the arbitrators can determine interest rates and remedies in case there were no terms, as it deems reasonable rate under the Late Payment Act, or else they would be determined under the England Arbitration Act. This assumes the meaning of the legal

⁵⁸⁸ [2010] EWHC 720 (TCC)

⁵⁸⁹ S9 of the Late Payment Act.

⁵⁹⁰ Ibid. see s9 (2) "regard shall be had to all the relevant circumstances at the time the terms in question are agreed".

interest rate as set forth in the in section 8 (1) and (4) of the Late Payment Act and section 23 of the Unfair Contract Terms, where the interest rate at least 8% per annum. However, these Acts only apply in the event if the parties have chosen such law. Thus, the applicable law to the dispute is a law that determines these rates and the validity of the contract and terms.

The previous laws are considered applicable laws to contracts related to interest.⁵⁹¹ Although that the Late Payment Act includes any debt that arises from any obligation under a contract, the debt in such Act does not carry statutory interest if the debt contains a sum that would be subject to interest other than statutory interest.⁵⁹² In addition, this law would not be applied and shall not be carried out if there is any rule of law in the same claim.⁵⁹³ However, it does not preclude the arbitrator from awarding damages, apart from this Act, because he has the power to award interest.⁵⁹⁴ Furthermore, this Act does not have effect with respect to a contract if it is governed by a part of the UK, according to choice of the parties, if there are no satisfactory relationship between the contract and that part of UK. In this case the applicable law is the foreign law.⁵⁹⁵ In contrast, this Act has effect with respect to a contract that is governed by a foreign law under the choice of the parties only if there is no satisfactory relationship between the contract and any other country except UK. In this case the applicable law is part of the UK.⁵⁹⁶

4.4.3.3 The most and real connection test

In one case,⁵⁹⁷ the court found that there was no sufficient connection between the contract and the English law, although the arbitration clause states that arbitration is subject to a London seat. However, the court found that the arbitration clause did not mean that the contract is subject to the law of England, as well as that the parties did not explicitly choose to make contract governed by English law, not even the rules of conflict of laws. Although a party sought to apply the Late Payment Act 1998 and the court indicated that there might be a connection, on the grounds that England is the place of performance of the obligation set forth and that one of the parties is of British nationality. In addition, some of the relevant parts of the business of the parties were to be implemented in England and the economic consequences of the delay in payment would occur in the UK. Despite the fact that the arbitral tribunal awarded a party 12.75% per annum interest of the original amount until the date of payment under the Late

⁵⁹¹ See 'Guidelines for Arbitrators on How to Approach the Making of Awards on Interest.' "There are three main cases where interest may be recoverable as of right: under an express term of the contract or trade usage; under the Late Payment of Commercial Debts (Interest) Act 1998; as damages for late payment."

⁵⁹² S3 (2) of the Late Payment Act. "A debt does not carry statutory interest if or to the extent that it consists of a sum to which a right to interest or to charge interest applies by virtue of any enactment (other than section 1 of this Act)."

⁵⁹³ S3 (3) of the Late Payment Act "A debt does not carry (and shall be treated as never having carried) statutory interest if or to the extent that a right to demand interest on it, which exists by virtue of any rule of law, is exercised."

⁵⁹⁴ S3 (2) of the Late Payment Act. "This subsection does not prevent a sum from carrying statutory interest by reason of the fact that a court, arbitrator or arbiter would, apart from this Act, have power to award interest on it."

⁵⁹⁵ See s12 (1) of the Late Payment Act 1998.

⁵⁹⁶ See s12 (1) of the Late Payment Act 1998.

⁵⁹⁷ *Martrade Shipping & Transport GmbH v United Enterprises Corporation* [2014] EWHC 1884 (Comm).

Payment Act, the Commercial Court did not also consider any of these factors to be able to constitute a relationship for the purposes s12 of such Act. As a result, the court confirmed Article IV of the Rome Convention which related with the applicable law in the absence of an explicit choice. Thus, the court found that the contract is not subject to English law due to the lack of explicit choice by the parties. However, English law gives debts more consideration than damages, where;

normally an express term will govern interest on debts, not on damages, ... where the applicable law of the contract is English law, it has historically been rare for a claimant to be able to claim interest as damages for late payment of a debt...[in some cases may allow to] a claimant to claim and prove his actual interest losses or other damage caused by late payment of a debt and an unparticularised and unproved claim simply for 'damages' will not suffice in English law.⁵⁹⁸

In the case where the parties choose the Late Payment Act, such Act would govern the terms of the contract or provide implied interest or remedies in case of failure of the parties to agree to their terms. In case these terms are governed by a foreign law, such law would determine the validity of contract. In contrast, in case of failure of choice of law by the parties, the task of choosing applicable law is delegated to the tribunal.

In brief, the interest rate and the time period are both procedural matters in England under its laws under the Arbitration Act, only if the contract terms are unfair as previously stated under UCTA under the rule of justices in case the contract is governed by English law. In England, for debt and late payment, there a minimum interest rate of at least 8%, as well as a maximum rate where it should not be including up to injustice or punishment. Compensation for delay in payment is not allowed except in the narrowest circumstances with proof of damage, because the interest for the delay is compensation for such delay. Under the agreement of the parties and the chosen law and under English law, remedies for compensation in sales contracts resulting from breaches of contract should not be unjust. It seems both damages and interest are procedural in international arbitration in case foreign law governs the contract and the English Arbitration Act governs the arbitral agreement.

4.4.4 U.S. law

Although the U.S. follows the CISG and Uniform Commercial Code (UCC), it was not able to unite such laws with regards to interest.⁵⁹⁹ Both codes are used unless contrary to

⁵⁹⁸ See 'Guidelines for Arbitrators on How to Approach the Making of Awards on Interest.'

⁵⁹⁹ See list of States that have adopted the UCC, and the codes that have been adopted under each state in 'Uniform Commercial Code Locator' (*Legal Information Institute*) <<https://www.law.cornell.edu/uniform/ucc>> accessed 20 October 2015.

fundamental public policy of the contrary or a state. However, neither bank codes nor sale codes of UCC refer to the interest rates or period with regards to late payment or debt, even the FAA does not address the power of arbitrators to award interest. The UCC provides interest and remedies for delayed payment or delivery of goods and damages.⁶⁰⁰ The UCC accentuates the rights of the parties to obtain interest for actual or anticipated damages caused by a breach of contract, but interest must be reasonable. In the event of no agreement, a sufficient remedy must be provided in case of failure with proof of actual damages.⁶⁰¹ The buyer is entitled to restitution of any amount by which the sum of his payments, such as 'the amount to which the seller is entitled by virtue of terms liquidating the seller's damages' or 'the amount or value of any benefits received by the buyer directly or indirectly by reason of the contract' plus interest.⁶⁰² The buyer is entitled to receive compensation for actual or anticipated damages caused by a justifiable delay in delivery of goods by the seller as it has resulted in a breach, thereby such damage is determined by the agreement under the reasonable amount or sufficient remedy. In case of failure such an agreement is then under the implied interest rate, which is 20% above the contract price.⁶⁰³ The parties can limit the compensation under their agreement, where can 'limit or alter the measure of damages recoverable' ... 'by limiting the buyer's remedies to return of the goods and repayment of the price'.⁶⁰⁴ However, they can 'resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive'. Thus, in case the remedy is large or such limitations cause it to fail in its main purpose, remedy may be considered implied under the code.⁶⁰⁵ Contracts including waivers of non-waivable statutory rights are considered contrary to substantive law in some states,⁶⁰⁶ while a waiver of lost profit is not. It may be limited or excluded unless such exclusion or limitation is unreasonable, and limitation 'in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not'.⁶⁰⁷ However, the UCC addresses the issue of delay in delivery of goods and other breaches, but refers in many places to the unreasonable terms or amount without giving a definition.⁶⁰⁸

This situation is similar to the English approach with regards to unconscionable clauses, where there is no definition of the term and it may relate to procedural matters. Unconscionable

⁶⁰⁰ See the Uniform Commercial Code-Sales, Article 2 of the UCC

⁶⁰¹ Art 2 (7) (18) of the UCC

⁶⁰² Art 2 (7) (18) of the UCC

⁶⁰³ Art 2 (7) (18) of the UCC

⁶⁰⁴ Art 2 (7) (19) of the UCC

⁶⁰⁵ Art 2 (7) (19) of the UCC

⁶⁰⁶ *Buckeye Check Cashing, Inc v Cardegna BT - US* (2006) 546 440 'that the provision waiving the statutory right to compensatory interest in Yates' form division order is unenforceable because it contravenes a clear, strong public policy ... which mandates that interest owners be paid interest on funds that they are legally entitled to receive. Accordingly, we reverse the Court of Appeals, affirm the district court, and remand for further proceedings consistent with this opinion.'; *Bridge Fund Capital Corp v Fastbucks Franchise BT - F 3d* (2010) 622 996 [999, 1003 and 1005].

⁶⁰⁷ Art 2 (7) (19) of the UCC

⁶⁰⁸ For more info, see Uniform Commercial Code.

terms may be only in case of bad faith and when the remedy is overstated. However, unconscionable clauses may cause courts to 'refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result'.⁶⁰⁹ Thus, 'the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting',⁶¹⁰ which is similar to legal action under the English law as mentioned. However, the lack of definition under different interpretations leads to a conflict of laws. In international arbitration a conflict would arise between the choice of law and the court in the arbitration seat, and between such a law and the court in the enforcement place in terms of judicial review, whether in the U.S. or under the choice of law of any state of the U.S, or between the States themselves.

4.4.4.1 Unconscionability theory

The lack of united meaning for unreasonable clauses also leads to a conflict of laws between the states of the U.S. with regards to the law applicable to the arbitral agreement and the merits of the dispute, and a conflict of laws in the validity of the arbitral agreement and in the main contract. Finally, the U.S. Supreme Court has identified three sets of circumstances that will render a clause as unreasonable:

(1) if their incorporation into the contract was the result of fraud, undue influence or overweening bargaining power; (2) if the selected forum is so "gravely difficult and inconvenient that [the complaining party] will for all practical purposes be deprived of its day in court"; or (3) if enforcement of the clauses would contravene a strong public policy of the forum in which the suit is brought, declared by statute or judicial decision.⁶¹¹

The most important one is last, when a contract contains unreasonable clause would affect the enforcement of the arbitral award. However, it varies from one law to another. In some States charging illegal interest is considered a violation of the law and according to public policy thereby it is an unreasonable clause, while in others it is not. In addition, the waiver of the non-waivable rights or compensation for more than the actual damages is considered unenforceable in some States.⁶¹² Thereby under this concept some laws of the U.S. also affect the validity of the arbitration agreement and the enforcement of arbitral award. In general, in some states of the U.S. charging above the legal interest rate, considered usury, is treated as a substantive matter, while late payments that compensate more than actual damages would be considered unreasonable or punitive;⁶¹³ they have no minimum interest for late payment, which is subject to the parties'

⁶⁰⁹ Art 2 (3) (2) of the UCC

⁶¹⁰ Art 2 (3) (2) of the UCC

⁶¹¹ *Williams v. CashCALL, INC.*, No. 14-CV-903 (E.D. Wis. Mar. 17, 2015).

⁶¹² See e.g. *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* [999,1005]; see also *Buckeye Check Cashing, Inc. v. Cardegna BT - US* [440].

⁶¹³ *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* [999].

agreement as it considers a procedural matter. In the U.S., compensation for damages as a result of breaches of contract in contracts of sale is procedural subject for the actual damages, similar to the Art 74 of CISG Convention.⁶¹⁴ In addition, the party is entitled to interest on late payments plus the actual damages, as is Art 78 of CISG Convention,⁶¹⁵ but it is a procedural matter under the parties' agreement. The parties may waive commercial losses as mentioned, but do not have the right to waive any logical right such as the delivery of goods or payment of price. Thus, in case of the delay in delivery of the goods, compensation is imposed in accordance with the agreement of the parties, or 20% of the contracted value if the parties failed to agree.

4.4.5 UAE law

In UAE law, late payments are governed under the agreement of the parties Articles 76 and 77 of the Federal Commercial Law 1993 unless the parties otherwise agreed as mentioned.⁶¹⁶ It seems that debts due to commercial loans differ from debt resulting from late payment in commercial other debt obligations in accordance with Articles 76 and 77. Article 81 defines the commercial obligation that indirectly includes both commercial loans and contracts of sale.⁶¹⁷ Thus, indirectly under Article 88,⁶¹⁸ a debt arising from a commercial obligation under a commercial loan is subject to Article 76 of the federal law, while a debt arising from a commercial obligation under a contract of sale resulting in late payment is subject to Article 77. As a result, the debt-based loan is limited to 12% but other debts are subject to the parties' agreement with no limited cap.⁶¹⁹

However, the injured party is entitled to receive compensation plus delayed interest with no need to prove damages. If there is proven bad faith the court can reduce such interest 'or it may not award any interest at all for the period of the unjustified prolongation'.⁶²⁰ Such a law

⁶¹⁴ "Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach. Such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract." see Art 74 of the CISG Convention.

⁶¹⁵ "If a party fails to pay the price or any other sum that is in arrears, the other party is entitled to interest on it, without prejudice to any claim for damages recoverable under article 74." See Art 74 of the CISG Convention.

⁶¹⁶ Art 88 of the Federal Commercial Law NO. (18) OF 1993

⁶¹⁷ "Where the commercial obligation is the delivery of a certain thing within a specific season or a time of the year, it shall be referred to the agreement between the two parties, in order to fix the time for delivery, and in case is no such agreement then to the custom prevailing in the country where the delivery is to take place." Art 81 (1) of the Federal Commercial Law NO. (18) OF 1993.

⁶¹⁸ "Where the commercial obligation is a sum of money which was known when the obligation arose and the debtor delays payment thereof, he shall be bound to pay to the creditors as compensation for the delay, the interest fixed in Articles (76) and (77), unless otherwise agreed." Art 88 of the Federal Commercial Law NO. (18) OF 1993.

⁶¹⁹ "A creditor is entitled to receive interest on a commercial loan as per the rate of interest stipulated in the contract. If such rate is not stated in the contract, it shall be calculated according to the rate of interest current in the market at the time of dealing, provided that it shall not exceed 12% until full settlement." Art 76 of the Federal Commercial Law NO. (18) OF 1993. "Where the contract stipulates the rate of interest and the debtor delays payment, the delay interest shall be calculated on basis of the agreed rate until full settlement." Art 77 of the Federal Commercial Law NO. (18) OF 1993. This reflects the outcome of the Court of Cassation in case no. 321 of 1999.

⁶²⁰ Arts 89 and 91 of the Federal Commercial Law NO. (18) OF 1993

provides remedies and procedural rules with regards to compensation for damages and the delay in delivery of goods and other matters.⁶²¹ In case of rescission,

the buyer shall return the item sold to the seller and [the] latter return to the buyer the instalments received after deducting therefrom charges equivalent to the benefit derived therefrom, in addition to an indemnity against the damage sustained by the item sold due to ordinary use thereof; all this unless there is a provision to the contrary in the sale contract and provided that the total amount received by the seller does not exceed the original price amount with its interests.⁶²²

As a consequence, in the UAE, the imposition of interest above the legal maximum interest rate in a loan contract is considered a violation of substantive law, while interest on late payments in commercial sales contracts or any compensation for damages is considered as procedural, thereby subject to the freedom of the parties under their agreement or otherwise failure to agree under the chosen law.

4.4.6 *Egyptian law*

It is likewise the situation in Egypt, where Art 231 of the Egyptian Civil Law allows the party to claim compensation plus interest. In addition, Art 151 of the same law allows compensation for damages even if such compensation is at a high rate.⁶²³ It is a procedural matter governed by the parties' agreement or otherwise by the law, and it is different whether or not it is related to administrative contracts and whether such compensation is for breaches of contract or actual damages.⁶²⁴ The Egyptian court may consider whether the arbitrators do not have a jurisdiction to award with regards to the enforcement and interpretation of the contract based on contractual responsibility or on the termination of the contract or on its nullity, only under the arbitral agreement, where arbitration is an alternative method to settle disputes and under such agreement to arbitration the arbitrators have brought their authority on the disputes. However, it has a limited interpretation with regards to the disputes that are subject of the arbitration.⁶²⁵

This may be more emphatic in case the dispute is administrative; in 2006 the CRCICA declined to award compensation for breach of contract based on 'Article 142 of the Egyptian Civil Code, which allowed an award of damages in a case of a void or cancelled contract'.⁶²⁶ However,

⁶²¹ Arts 103, 150, 292 and 316 of the Federal Commercial Law NO. (18) OF 1993

⁶²² Art 116 of the Federal Commercial Law NO. (18) OF 1993; see for more info USA International Business Publications, *United Arab Emirates Business Law Handbook: Strategic Information and Laws* (Int'l Business Publications 2012).

⁶²³ See Gotanda 48.

⁶²⁴ See e.g. G Wang, *International Investment Law: A Chinese Perspective* (Taylor & Francis 2014) 470; see also JDMAM Ismail, *Globalization and New International Public Works Agreements in Developing Countries: An Analytical Perspective* (Ashgate Publishing Limited 2013) 83–84.

⁶²⁵ See the discussion of Cairo Court of Appeal on July 27, 2003 No. 12 of the 120th judicial year.

⁶²⁶ Where 'The Defendant contended that the Claimant had committed fraud and accordingly the Defendant was entitled to cancel the concession contract. The Tribunal chose not to rule on the Claimant's claim for breach of contract.' see *Malicorp Ltd v Government of the Arab Republic of Egypt & Ors* [2015] EWIIC 361 (Comm), available at

the Cairo Court of Appeal set aside the Cairo Award on 5 December 2012.⁶²⁷ Thus, 'the English Commercial Court refused enforcement of a foreign arbitral award on the grounds that the award had already been set aside by a properly recognizable foreign judgment and the tribunal had acted in such a way as to render the Defendant unable to present its case'.⁶²⁸ In some cases, compensation is awarded providing damages can be proven.⁶²⁹ Compensation is allowed under Egyptian law whether for breaches of contract or others and it is a procedural matter under the parties' agreement, where 'the literal wording of an agreement should be strictly adhered to insofar as such wording is manifestly unequivocal and definitely unambiguous to the extent that it essentially reflects the parties' common intention'.⁶³⁰ Compensation for a breach of contract is practical in approach for all contracts under the parties' agreement, the actual damages or the law.⁶³¹

In UAE and Egyptian law, the maximum interest rate is limited to loans, while compensations with regards to damages are not limited and are subject to the parties' agreement. Under Saudi law and therefore *Sharia* law, interest-based loans are limited, while compensation for damages is limited to the actual damages or to the parties' agreement with the exception of the loan and debts. However, there is no limitation on compensation with regards to a breach of contract under the parties' agreement.

4.5 Punitive damages

In international arbitration, compensation for damages is the most common type of award, which includes punitive damages and incidental payments for paying a disputed debt.⁶³² The punitive damages may have two functions, such as punishment and compensation. Punitive damages include civil penalties for violations, but not criminal penalties. This nature of penalty was a justification why the courts should decide such a matter as a state organ. However, breaches of contract are not linked to a time period, thus in such cases the compensation is either according to clause or as a punishment by the arbitrators. If there is no punitive clause in the contract, the arbitrator is not entitled to impose punishment unless provided for by the applicable law. If there is a punitive clause, the arbitrator is obliged to implement the contract and such clause, at

<http://www.mcnaarchambers.com/media/documents/201504/ENGLISH_COMMERCIAL_COURT_SETS_ASIDE_ORDER.pdf>

⁶²⁷ *Malicorp Ltd v Government of the Arab Republic of Egypt & Ors* [2015] EWHC 361 (Comm)

⁶²⁸ *Malicorp Ltd v Government of the Arab Republic of Egypt & Ors* [2015] EWHC 361 (Comm)

⁶²⁹ 'Claimant failed to substantiate its compensation claims or prove the three elements of liability (breach or fault, harm or damage, and the causation).' See Albert Jan van den Berg (ed), 'Contractor (Egypt) v. Employer (Egypt), Final Award, CRCICA Case No. 730 of 2011', *Yearbook Commercial Arbitration 2013 - Volume XXXI III, Yearbook Commercial Arbitration, Volume 38*, vol 38 (Kluwer Law International 2013)49; see also 'Hotel Company v. Construction Company, Final Award, CRCICA Case No. 730/2011, 18 February 2013 in Arbitral Awards of the Cairo Regional Centre for International Commercial Arbitration' 395.

⁶³⁰ Berg, 'Contractor (Egypt) v. Employer (Egypt), Final Award, CRCICA Case No. 730 of 2011' 41.

⁶³¹ *Parsons & Wh. Ov. Co., Inc. v. SOCIETE G. DE L. DU P.(R.)*, 508 F.2d 969 (2d Cir. 1974).

⁶³² Martin and Green 159.

whatever interest rate because it is a procedural matter according to the parties' agreement. In cases of late payment or delayed delivery, if there is a remedy then it should be applied under the applicable law, or if not then the contract is implemented under the applicable law to contract directly where some laws apply at the implied interest rate. In loan contracts, some laws allow interest rates under the parties' agreement unless it is in excess of the upper limit of the interest rates, while others allow the imposition of interest rates with no limit, thereby the rate is subject to the applicable law for the contract.

In Common Law in the U.S. the punitive damage may be awarded in case of a breach of contract.⁶³³ It is argued that the punitive damages are contrary to public policy and non-arbitrable and unenforceable.⁶³⁴ However, in New York City, punitive damages are not arbitrable,⁶³⁵ and in California law they are unreasonable and unenforceable,⁶³⁶ while under US federal law such a matter is arbitrable in the case the parties agreed clearly to the power and authority of arbitrators for awarding punitive damages.⁶³⁷ However, punitive damages can be arbitrable if the claim for punitive damages was not prejudicial in case the parties have agreed on such a matter before submission to arbitration.⁶³⁸ Further, the courts with regards to punitive damages ruled in favour of arbitration if the parties have agreed.⁶³⁹ Thus, in U.S. federal law, arbitrators have power to make awards of monetary and punitive damages.⁶⁴⁰

⁶³³ See e.g. Georges Cavalier, 'Punitive Damages and French International Public Policy' in R. Sturmer and M. Kawano (ed), *Comparative Studies on Business Tort Litigation* (Mohr Siebeck 2011) 221–232

⁶³⁴ GI Zekos, *International Commercial and Marine Arbitration* (RoutledgeCavendish, Taylor & Francis Group 2008) 61; Carbonneau, 'Revolution in Law through Arbitration, The Eighty- Fourth Cleveland-Marshall Fund Visiting Scholar Lecture' 239; Albert Jan van den Berg, *Yearbook Commercial Arbitration* (Kluwer Law International 2004) 999,1003; D Laycock, *Modern American Remedies: Cases and Materials* (Aspen Law & Business 2002) 732–736; See also *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F.* 3d [999,1003]; See *Laminoirs-Trefileries-Cableries de Lens SA v Southwire Co.*, 484 F Supp 1063 (ND Georgia 1980) 'US Federal District Court refused to enforce a foreign arbitral award under the New York Convention on public policy grounds because the arbitrators' increase of interest rates by an additional 5% would amount to punitive damage and would not be enforceable'.

⁶³⁵ See *Garrity v. Lyle Stuart, Inc.*, 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976).

⁶³⁶ *Buckeye Check Cashing, Inc. v. Cardegna BT - US; Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F.* 3d.

⁶³⁷ See *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 115 S. Ct. 1212, 131 L. Ed. 2d 76 (1995).

⁶³⁸ See *Rush v. Oppenheimer & Co.*, 779 F.2d 885, 887 (2d Cir. 1985) at [890].

⁶³⁹ The United States Court of Appeals for the Eleventh Circuit in *Willoughby Roofing & Supply Co. v. Kajimia International*, 776 F.2d 269 (11th Cir. 1985), affirming 598 F. Supp. 353 (M.D. Ala. 1984), held "our task is to resolve all doubt in favour of the arbitrator's authority to award a particular remedy."; The U.S. Supreme Court in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 63 U.S.L.W. at 4195 (1995), held "... we have previously held that the FAA's pro-arbitration policy does not operate without regard to the wishes of the contracting parties."... "The Court found that the rules incorporated in the contract allowed punitive damages, thus at most, the New York choice-of- law provision introduced an ambiguity into the contract, which should be resolved in favour of arbitrating the punitive damages issue"; In *Volt Information Sciences, Inc. v. Board of Trustees of the Leland Stanford Junior University*, 489 U.S. 468, 478-479, 109 S. Ct. 1248, 1255, 103 L.Ed.2d 488 (1989), the Supreme Court held that the "parties are generally free to structure their arbitration agreement as they see fit.". The federal district court in *Willis v. Shearson/ American Express Inc.* 569 F. Supp. 821 (M.D.N.C. 1983), held that a claim for punitive damages was arbitrable due to there was no "public policy reason persuasive enough to justify prohibiting arbitrators from resolving issues of punitive damages submitted by the parties".

⁶⁴⁰ See *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989); see also *Spery Intern. Trade v. Government of Israel*, 689 F.2d 301 (2d Cir. 1982).

A court ruling distinguished between punitive damages in tort and a breach of contract, thereby ruling in favour of arbitration,⁶⁴¹ where punitive damages are awarded in what are essentially breach of contract cases.⁶⁴² In England, the concept of civil and criminal was not divided. Dahlberg and Welsh observe that 'there is no express rule as to whether arbitrators can award punitive or exemplary damages'.⁶⁴³ However, parties are free to agree on interest rates and remedies to the contract that would be awarded by the arbitrators,⁶⁴⁴ unless the parties were not agreed then the aforementioned are determined by the arbitrators themselves.⁶⁴⁵ Accordingly, under English law the arbitrators may award punitive damages, where they have the power to award by default. This is not allowed when English law governs the contract and dispute. However, it would be enforced when the foreign arbitral award is considered under an applicable foreign law.⁶⁴⁶

Some arbitration laws limit the ability of the arbitrators to award compensation unless for breach of contract cases.⁶⁴⁷ In Civil Law the concept of punitive damages is hardly known, whether it is related to a breach of contract or not. It is argued that Civil Law countries, including France, do not allow punitive damages.⁶⁴⁸ In principle, under the French international public policy, punitive damages are no longer considered non-arbitrable.⁶⁴⁹ The differences between such legal systems and the conflicting interpretation of breaches of contract has led to confusion and concern. In general, the law applicable to the merit of dispute is the most important element in determining the arbitrator's approach to awarding interest⁶⁵⁰ and compensations.

⁶⁴¹ *Episcopal Diocese v. Prudential Securities*, Florida Ct App 2006, 'This clause binds the undersigned to submit to arbitration all claims including those which could otherwise be brought in a judicial forum and those which could be joined to other non-arbitrable claims'

⁶⁴² E Allan Farnsworth, 'Punitive Damages in Arbitration' in Loukas A Mistelis and Julian DM Lew (eds), *Arbitration Insights: Twenty Years of the Annual Lecture of the School of International Arbitration, Sponsored by Freshfields Bruckhaus Deringer, International Arbitration Law Library, Volume 16* (Kluwer Law International 2007) 91.

⁶⁴³ Andrea Dahlberg and Angeline Welsh, 'Arbitration – Country Guides, ENGLAND AND WALES' (2012) 13.

⁶⁴⁴ See sections 48 (1) and 49 (1) of the Arbitration Act, 1996.

⁶⁴⁵ See sections 48 (2-5) and 49 (2-6) of the Arbitration Act, 1996.

⁶⁴⁶ As mentioned above, for some info see e.g. John Yukio Gotanda, *Supplemental Damages in Private International Law: The Awarding of Interest, Attorneys' Fees and Costs, Punitive Damages and Damages in Foreign Currency Examined in the Comparative and International Context* (Kluwer Law International 1998) 199.

⁶⁴⁷ Martin and Green 159.

⁶⁴⁸ Martin and Green 159–160 Civil law legal systems generally limit recovery of damages in private actions to an amount that restores a party to its pre-injury condition' and so do not allow the award of punitive damages. Countries that do not allow punitive damages include France...'; Karen Halverson Cross, 'Letting the Arbitrator Decide Unconscionability Challenges' (2011) 26 The John Marshall Institutional Repository <<http://repository.jmls.edu/cgi/viewcontent.cgi?article=1350&context=faepubs>>; Carbonneau, 'Revolution in Law through Arbitration. The Eighty- Fourth Cleveland-Marshall Fund Visiting Scholar Lecture' 239–265; Zekos 61; Georges AJ Cavalier and Jean-Sebastian Queguiner, 'Punitive Damages and French Public Policy' [2007] Available at SSRN 1174363; Berg, *Yearbook Commercial Arbitration* 965; See also *Higher Regional Court of Munich, decision - SchiedsVZ*.

⁶⁴⁹ Georges Cavalier, 'Punitive Damages and French International Public Policy' in R. Sturmer and M. Kawano (ed), *Comparative Studies on Business Tort Litigation* (Mohr Siebeck 2011) 221–232.

⁶⁵⁰ Hunter and others.

For loan contracts under *Sharia* law, there are many views on whether this compensation is punitive or for damages.⁶⁵¹ It is generally agreed that for damages compensation equal to damages is required, but they disagree on who shall estimate such compensation.⁶⁵² It is also not true from the above evidence that compensation should just be for punishment and to divert money to the state treasury. In this case, the damage is still on the injured party, and he has not received compensation for the damage that injury him. It may be a punishment or penalty for the procrastinator but still there is an aggrieved party. Thus, from the above, it shows that the compensation is not intended for itself but for the damage, and that the public interest requires it, however it must be fair and acceptable, and equal to the harm itself, also without any previous conditions.

4.6 Conclusion

Interest may be related to loans, late payment and breaches of contract, subject to the laws of interest and usury of difference jurisdictions. As the research has shown, there is a confusion between compensation, late payment, punitive damages and illegal interest. In loan contracts, charging illegal interest above the maximum interest rate is considered usury under the laws of most of the countries examined, and under *Sharia* law as it is

⁶⁵¹ There are differing opinions relating to Sheikh Abdullah Ibn Mniea's statement, which also raises several questions. E.g., does the money paid to the creditor come from punishment through an injunction or is it a punishment to fix real harm? Further to this are the questions of how the value of the compensation should be estimated, and who has the power to implement the punishment? Once again, this issue has two-opinion; The first opinion states that the fine or the compensation, which is a punishment of money, is not required to be equal to the damage or loss of profits, and is a view opined by Sheikh Abdullah bin Mniea. He also commented on Sheikh Mustafa Zarqa: "With the agreements with the Sheikh in the lead, but I see that the financial penalty only for punishment, it is not for compensation". See Sheikh Abdullah bin Suleiman bin Mniea, in his *Fatwas and Research* (3/240). However, then said: "But we say that as punishment not only for compensation dependency." See *Ibid*, 3/252. He said in another place: "The bottom line: if we consider what the creditor takes from the debtor as only compensation, then this consideration will refer the matter to the prohibition ...If we consider that the creditor loses his money due to the procrastination, then this is a penalty upon the debtor, which has no link or relationship with the size of damage to the creditor, but adapted depending on what requires deterrence and rebuke, and this consideration is true". *Ibid*, 3/264

⁶⁵² Sheikh Mustafa Zarqa says: that the judiciary alone is the owner of the only authority to estimate the compensation and assess the damage caused to the creditor. It is the responsibility of the judiciary to estimate the cause of the delay of the debtor. Thus, it is not permissible, the agreement in advance between the creditor and the debtor, and to give an estimate of damage as a result of the delay. However, the estimate of damage should be as much as the expected loss of profit at the lowest normal limits, in the way of general trade, which if he takes his money and invested legitimately in Islam such as *mudaraba*, *musharaka*, *Murabaha* and others, without consideration to the bank interest rate. Thus the Court relies the estimate of the opinion of the people with experience in this regard. After the creation of Islamic banks, the Court can rely on the estimation of compensation based on what is distributed from the annual profits of Islamic banks. See Mustafa bin Ahmed Al Zarqa in his article: about the permissibility of the compulsion of debtor "procrastinator" to compensate the creditor, published in the *Journal of Economic Studies doctrinal*, p 20, c: 3 Edition: 2, 1417 H (1996). Adherer believes: "that an agreement may be reached between the creditor and the debtor - the client and the bank - to compensate for the actual real damage in advance. This will be appreciated on the basis of the actual profit achieved by the creditor - Bank - in the period in which the debtor delayed in meeting the debt". According to sheikh Shabelle: "That the compensation should be as much as the profit that the procrastinator has got, as a result of his trade with money during the period of procrastination". See Shabelle, *Method of accounting for Murabaha*, p. 120 and banking services, (2/608).

called *Riba*. However, in *Sharia* the interest rate itself is not tolerated and even 1% interest is considered illegal and as *Riba*.

Compensation is allowed in most countries, but for damages it is required to be equal to the actual damages in some countries, or according to the parties' agreement in others, or both. For late payment, it is considered illegal with regard to debt under *Sharia* law unless there is a damage with no requirement by the parties. It is limited to the maximum interest rate and subject to the parties' agreement, or subject to the implied interest rate under some jurisdictions. Punitive damages are subject to the parties' agreement, the applicable law to the dispute, or to the authority of the arbitrator.

These conflicts of laws and differences would have an effect on the determination of the legality of interest in the contract under the applicable law and may have an impact on the validity of the contract or the arbitration agreement within the interpretation and the application of the NYC under different jurisdictions. However, conflicts may further arise under the seat of arbitration between the applicable law to the arbitration agreement, the law of the arbitration seat with regard to usury or interest rates, the non-arbitrable matters, the validity of the arbitration agreement and the authority of the arbitrator.

Furthermore, the influence of the parties' clauses on the validity of the contract may affect the validity of the arbitration clause or submission to arbitration, or the scope of the arbitration. Conflicts may also arise between the law applicable to the dispute and the law of the enforcement place, regarding the enforceability of the award containing interest, where there are also confusions between violation of public policy, illegal interest and non-arbitrability under NYC. Such issues will be addressed in Chapter Five.

Chapter 5. Arbitrability of interest

5.1 Introduction

The concept of arbitrability is very complex in the law and practices, especially when it comes to interest. Interest claims consider non-arbitrable matters and may give effect to the validity of the arbitration agreement, unless the award goes beyond the scope of such agreement under some circumstances in some jurisdictions as direct or indirect non-arbitrability. Under these countries, the arbitration agreement would be invalidated directly under the substantive and procedural rules, from the incapacity of the parties under bankruptcy, or indirectly from the invalidity of a contract that contains illegal interest. Bankruptcy is also considered a non-arbitrable matter. Interest matters are related to substantive or procedural laws under countries discussed in this research. Such laws give effect to arbitrability, whether under Art II or Art V of the NYC. In these countries, non-arbitrability takes a different approach related to public policy or outright non-enforceability.

Conflicts arise in many countries in the to the jurisdiction of the arbitral tribunals regarding interest rates, accrual periods and judgement dates. Some national courts intervene in the jurisdiction of the arbitral tribunals, which affects the arbitration process and enforcement. However, some courts in these countries require that the parties should agree expressly to the arbitrability, the scope of the arbitration, the interest rate and period and the punitive damages, otherwise, the matter will be non-arbitrable. Some courts also intervene in the determination of the law applicable to the contract and the arbitration agreement, which leads to a conflict of laws between the law of the arbitration agreement, the law applicable to the contract, the law applicable to the contract and the law of the enforcement country.

5.1.1 Arbitrability

A dispute cannot be submitted to arbitration if it is non-arbitrable as it may include matters directly related to the public interest, as a matter of law.⁶⁵³ The concept of arbitrability reflects the meaning of the matters that are eligible for settlement by arbitration.⁶⁵⁴ However, arbitrability may reflect a negativity against party autonomy.⁶⁵⁵ There are similarities in the

⁶⁵³ Thomas E Carbonneau, *Arbitration in a Nutshell* (Thomson/West 2007) 14.

⁶⁵⁴ Pieter Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges* (the International Council for Commercial Arbitration 2011) <http://www.arbitration-icca.org/media/1/13890217974630/judges_guide_english_composite_final_jan2014.pdf> 'those matters deemed non-arbitrable' because they belong exclusively to the domain of the courts'.

⁶⁵⁵ Conn Bernice and Michael Geibelson, 'We Agreed to What?! How the Selection of an Arbitration Clause Can Impact a Client's Legal Rights' *Business Law News* (2007) <<http://www.robinskaplan.com/resources/articles/we-agreed-to-what-how-the-selection-of-an-arbitration-clause-can-impact-a-client-s-legal-rights>> 'for the most part, arbitrability involves two interrelated concepts: (1) whether the court or the arbitrator should decide the scope of the parties' agreement to arbitrate, and (2) whether the parties agreed to arbitrate their present dispute.'; see e.g. Edward M Morgan, 'Contract Theory and the Sources of Rights: An Approach to the Arbitrability Question' (1986) 60 S.

meaning of non-arbitrability and non-arbitrable terms, which both mean that the dispute is subject to the jurisdiction of the courts and not subject to the jurisdictions of the arbitrators.⁶⁵⁶ However, there is an overlap of these terms which may cause confusion among researchers and arbitrators.⁶⁵⁷ According to Mistelis and Brekoulakis the issue is mere differences in the terms and the uses.⁶⁵⁸

However, there are some who observe that '[a]rbitrability refers only to whether specific classes of disputes are barred from arbitration because of the subject matter of the dispute, whereas in the United States "arbitrability" also refers to the complicated balance between courts and arbitrators regarding who should be the initial decision-maker on issues such as the validity of the arbitration agreement'.⁶⁵⁹ Thus, the Mistelis and Brekoulakis observe that 'terminology may not bear great importance, it is possible to argue that lack of arbitrability may also be considered as a ground leading to incapability of the arbitration being performed'.⁶⁶⁰ The merit of dispute may be non-arbitrable or arbitrable but may be non-arbitrable under the arbitration agreement.⁶⁶¹ As a result, the concept of non-arbitrability is more general in the meaning and would cover the concept of non-arbitrable.⁶⁶²

Some believe that the question of arbitrability can be divided to two forms, subjective arbitrability and objective arbitrability. Subjective arbitrability reflects the substantive matters and objective arbitrability refers to procedural matters.⁶⁶³ In this thesis, the terms arbitrable and arbitrability are used instead for clarity.⁶⁶⁴ Arbitrable refers the type of dispute and arbitrability refers to other questions that affect the consideration of the matter under arbitration. This provides

Cal. L. Rev. 1059, 1059 'The arbitrability doctrine addresses this distinction between State process and autonomous adjudication of rights, by designating the kind of claims that fall within the scope of agreement for private dispute resolution.'; For e.g. see *Tricon Energy Limited v. Vinmar International, Ltd* 'if the arbitrators awarded a non-statutory rate, they did so based on the parties' submission of the issue to them, not on their own authority. An arbitration panel may determine whether the parties have sufficiently contracted for their own rate and, if they have, indicate that rate should be applied'.

⁶⁵⁶ There are common denominators between non-arbitrable and non-arbitrability concepts. See John Savage and Emmanuel Gaillard, *Fouchard Gaillard Goldman on International Commercial Arbitration* (John Savage and Emmanuel Gaillard eds, Kluwer Law International 1999). Arbitrability "where the subject matter of the dispute that brought to arbitration that can not be settled by arbitration".

⁶⁵⁷ See Loukas A Mistelis and Stavros L Brekoulakis, *Arbitrability: International and Comparative Perspectives* (Kluwer Law International 2009) 4,5,6-31.

⁶⁵⁸ Mistelis and Brekoulakis 69-70.

⁶⁵⁹ See Laurence Shore, 'Defining "Arbitrability": The United States vs. the Rest of the World' (2009) 15 *New York Law Journal* <<http://www.gibsondunn.com/publications/documents/shore-definingarbitrability.pdf>> accessed 6 October 2015.

⁶⁶⁰ see Mistelis and Brekoulakis 94.

⁶⁶¹ For more info see Mistelis and Brekoulakis; Shivesh Aggarwal, 'Arbitrability Of Fraud In Light Of World Sport Group (MAURITIUS) LTD. Case' [2014] *Arbiter Dictum* 'The concept of arbitrability involves what types of disputes can be submitted to arbitration; and what specific classes of disputes are exempted from arbitration proceedings and belong exclusively to the domain of state courts'.

⁶⁶² The non-arbitrability refers to the submission of the dispute to the courts rather the arbitration, because of a defect in some of substantive and procedural matters, while non-arbitrable refers to the substantive matters.

⁶⁶³ See See Kronke 220; see Mistelis and Brekoulakis; see also Redfern 148.

⁶⁶⁴ Courts usually use "arbitrability" to refer to the quality or state of being arbitrable. See, e.g., *Texoma Natural Gas Co v OIL WORKERS IU, ETC BT - F Supp* (1943) 58 132. Nevertheless, arbitrability is not defined in Black's Law Dictionary, Webster's Third New International Dictionary, or the Oxford English Dictionary. Although the word arbitrable can be traced back nearly five hundred years, see Oxford English Dictionary (2d ed. 1989) 601-602.

a full detailed study on the NYC, which states directly that the court would not recognize or enforce the arbitration agreement, including non-arbitrable matters,⁶⁶⁵ or indirectly that the arbitration agreement cannot be enforced due to non-arbitrability.⁶⁶⁶

The confusion does not only arise from the arbitrability concept, but also from the application of Arts II and V of the NYC. Consequently, there are some issues that occur, such as determining either the scope of dispute or the law applicable to the arbitration agreement or contract. The conflict also arises in the case that the arbitration agreement is invalid,⁶⁶⁷ limiting of the authority and power of the arbitrator⁶⁶⁸ and the effect of law of the arbitration seat and the law of the enforcement place,⁶⁶⁹ and possibly duplicating the judicial review.⁶⁷⁰ In this chapter we will address the recognition and enforcement of arbitration agreements and arbitral awards with respect to arbitrability of compensation or awarding of interest.

5.1.2 *Recognition and enforcement stages*

As mentioned, there are two stages with in the recognition and enforcement of foreign arbitration agreements and foreign arbitral awards.⁶⁷¹ Similarly, the recognition and enforcement also go through two processes, first recognition and enforcement with regards to the arbitration agreement,⁶⁷² and second the recognition and enforcement of the arbitral award. The arbitration agreement will not be recognized and enforced if such agreement refers to subject matter that is not eligible for settlement by arbitration under Art II (1) as directly non-arbitrable. In addition, the arbitration agreement is invalid under some controversies⁶⁷³ according to Art II (3), or indirect non-arbitrability. A link is made between Art V(1) (a) and Art II (3) where the rules of arbitrability are given and the obligation of the signatory States to uphold a valid arbitration agreement is defined.

⁶⁶⁵ According to Art II (1) of NYC, A State signatory to the Convention would be subject to some questions, such as non-arbitrability. See Born (n 22) 567; Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges* 'A court may be seised of the plea that the arbitration agreement concerns a subject matter not 'capable of settlement by arbitration' for the purposes of Article II (1), and therefore, should not be recognized or enforced.'

⁶⁶⁶ Art II (3) of the NYC and the legal effect of Art V (1) (a) of NYC.

⁶⁶⁷ Whether either the agreement is invalid according to act (II) and V (1) or in case the agreement/underlying contract includes usury or interest.

⁶⁶⁸ Is the arbitrator has the ability to decide the matter is arbitrable/arbitrability, or the ability to chose of the law/applicable law and any limitation of his freedom and authority.

⁶⁶⁹ Which give effect on the award and the arbitrable question, is the forum court has an ability to review the agreement/award, and ensure of the arbitrability question.

⁶⁷⁰ The court of arbitration seat, the court of enforcement place and overlap between them

⁶⁷¹ The first phase is recognition and enforcement of the arbitration agreement; the second one is recognition and enforcement of the arbitral award, see Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges*.

⁶⁷² Richard A Mann and Barry S Roberts, *Essentials of Business Law and the Legal Environment* (Cengage Learning 2015) 64; Claudia Salomon and Samuel de Villiers, 'The United States Federal Arbitration Act: A Powerful Tool for Enforcing Arbitration Agreements and Arbitral Awards' [2014] Latham & Watkins LLP; Berg, 'New York Convention of 1958: Refusals of Enforcement.'

⁶⁷³ See Mistelis and Brekoulakis 325.

An arbitral award would not be recognised and enforced if the subject matter also is not eligible for settlement by arbitration under the law of the enforcement place under Art V(2) (a). Furthermore, the arbitral award would not be recognised and enforced if the arbitral agreement contains disputes falling within the scope of non-arbitrability for the same legal effect of Art II (3), in case the award goes beyond the scope of the agreement under Art V (1) (c). Whether a matter is arbitrable would be determined according to the type of the disputes under the seat of arbitration and under the place of enforcement under Art II (3) and V (2) (a) of NYC. The question of arbitrability would be determined in accordance with the arbitration agreement, the applicable law to the arbitration agreement, the applicable law to the contract, the law of the seat of arbitration, and the principle of separability of the arbitration agreement.

5.2 The enforcement of the arbitral agreement; Non-arbitrable matters

Article 7 of the Model Law parallels Art II of the NYC, giving a definition of an arbitration agreement as covers disputes which have arisen or which may arise, but does not identify the type of such disputes. Each relevant court can decide on matters that are considered arbitrable or non-arbitrable, according to its own social, economic and political policy.⁶⁷⁴ Non-arbitrable matters or substantive arbitrability 'refers to the situation where the subject matter itself is not arbitrable even if there might be nothing wrong with the validity of the arbitration agreement per se'.⁶⁷⁵ Although the list of non-arbitrable matters has diminished with the passage of time, as a result of the widening and growing acceptance of arbitration and a distinction between domestic and international arbitrations,⁶⁷⁶ non-arbitrable matters are vary from one jurisdiction to another, leading to conflicts between the laws with regards to what the law determines is non-arbitrable.

There are controversies under different jurisdictions on non-arbitrable matters but in countries that are arbitration-friendly, such as Switzerland and Germany, disputes related to economic interests are all deemed arbitrable.⁶⁷⁷ Most countries refer to the matters of divorce and criminal offences that are non-commercial disputes are non-arbitrable. Some countries refer to the matter of bankruptcy, punitive damage, and usury as non-arbitrable, but others consider only illegal interest to be non-arbitrable. The question remains under any law how the issue of non-arbitrable would be determined. The non-arbitrable question can be determined under the law of the country where the application for recognition and enforcement is made.⁶⁷⁸ The relevant non-

⁶⁷⁴ Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges*.

⁶⁷⁵ Michael Hwang and Shaun Lee, 'Survey of South East Asian Nations on the Application of the New York Convention' (2008) 25 *Journal of International Arbitration* 873.

⁶⁷⁶ Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges* 63.

⁶⁷⁷ Frank-Bernd Weigand, *Practitioner's Handbook on International Commercial Arbitration* (OUP Oxford 2009); Savage and Gaillard: *Higher Regional Court of Munich, decision - SchiedsVZ*. See also Art 177 (1) Federal Statute on Private International Law, "Any dispute of financial interest may be the subject of an arbitration".

⁶⁷⁸ Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges* 105.

arbitrable rule should be decided by an arbitral tribunal according to its authority or a forum court in the arbitral seat, and only in very rare cases would the forum court have the right to deny this effect when the decision is contrary to a mandatory law.⁶⁷⁹

5.2.1 *Interest-based loans*

Among various types of disputes, interest-based loans are one of the important matters where they are related to usury in case such interest overrides the legal interest rate. In England, the English Arbitration Act 1996 does not list the matters that are non-arbitrable, but says disputes in a commercial nature are arbitrable.⁶⁸⁰ However, the Act expressly refers to interest, which means it is arbitrable, but does not specify whether an interest-based loan is a form of usury or illegal interest. In contrast, the non-arbitrable matters are considered case-by-case basis.⁶⁸¹ Similarly, in France, the question of arbitrable is not clear,⁶⁸² but it is argued that interest claims are a form of usury not arbitrable under French law.⁶⁸³ However, in international commercial arbitration neither the law applicable to the arbitral agreement nor the law applicable to the dispute should be contrary to the international public policy.⁶⁸⁴ In the U.S., the FAA is not self-executing and it does not define or specify the controversies that are subject to arbitration.⁶⁸⁵ In addition, the FAA requires courts to enforce arbitration agreements in contracts involving interstate commerce.⁶⁸⁶ However, under the law of some states, illegal interest or usury is not arbitrable,

⁶⁷⁹ Born (n 22) 606–607.

⁶⁸⁰ The Arbitration Act, 1996, s6 (1) provide that both contractual and non-contractual disputes may be submitted to arbitration. Commercial disputes arising under a valid arbitration agreement are generally arbitrable. However, s.81 (1)(a) England Arbitration Act does not mention or determine matters that are arbitrable but matters that are considered non-arbitrable under English Act involving family law and criminal matters, which deemed non-arbitrable; see also William W Park, 'The United Kingdom and the UNCITRAL Model Law; The Mustill Committees' Consultative Document of October 1987 on the Model Law' (1987) 3 LCIA 'Such matters as are not arbitrable in England (e.g. civil status, liability for criminal offences, etc) lie almost wholly outside the commercial field'. See also Mustill and Boyd, *Law and Practice of Commercial Arbitration in England*, (2nd ed) (1989), 149-150 cited in Albert Jan van den Berg, *Yearbook Commercial Arbitration* (Kluwer Law International 2004) 402. 'English law has never arrived at a general theory for distinguishing those disputes which may be settled by arbitration from those which may not. [...] the types of remedies which the arbitrator can award are limited by considerations of public policy and by the fact that he is appointed by the parties and not by the state'

⁶⁸¹ See Zheng Sophia Tang, *Jurisdiction and Arbitration Agreements in International Commercial Law* (Taylor & Francis 2014) 94. See also *Fulham Football Club (1987) Ltd v Richards and another* [2012] Ch 333, (Patten LJ stated) [40] 'it is necessary to consider in relation to the matters in dispute in each case whether they engage third party rights or represent an attempt to delegate to arbitrators a matter of public interest which could not be determined within the limitations of a private contractual process'.

⁶⁸² Weigand 45 'In some jurisdictions, there is either no general definition of arbitrable disputes (as in England), or the concept applied is rather vague and entails difficult problems of definition and interpretation (as in France)'.

⁶⁸³ Jan Paulsson, *The Idea of Arbitration* (Oxford University Press 2013) 135–137.

⁶⁸⁴ See Bars and Kaminsky.

⁶⁸⁵ GAVIN J GADBERRY and DAN L SCHAAP, 'Federal Arbitration Act ('Faa') Preemption Of State Law' (2004) 5 <<https://www.international-arbitration-attorney.com/wp-content/uploads/federal-arbitration-act-faapreemption-of-state-lawgavin-j-gadberryyanddan-l-schaapu.pdf>>.

⁶⁸⁶ See 9 U. S. C. § 1 *et seq*; see also *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989) at [481]. 'Not only does the FAA require the enforcement of arbitration agreements, but we have held that it also establishes substantive federal law that must be consulted in determining whether (or to what extent) a given contract provides for arbitration.' id 485

which is similar to the French approach.⁶⁸⁷ Consequently, some courts would refuse to enforce the arbitration agreement or the contract that contains usury⁶⁸⁸ where it is non-arbitrable.⁶⁸⁹

The Saudi Arbitration law emphasizes the enforcement of arbitration agreements unless the agreement is inconsistent with *Sharia* law.⁶⁹⁰ Further, arbitration is not permitted where no conciliation is permitted.⁶⁹¹ However, Saudi Arbitration law does not determine the matters that are non-arbitrable or whether that the claims related to the contract involving *Riba* are considered within the jurisdiction of court or to the arbitrators. There are some arguments with regards to claims involving prohibited matters such as *Riba*, which will be non-arbitrable according to these views (see Chapter Four). Aljazy observes that interest is non-arbitrable in *Sharia* law.⁶⁹² This is supported by El-Ahdab, who observes that matters related to “the Rights of *Allah*” and public policy cannot submit to arbitration and the scope of arbitrator's authority is limited to matters that can be subject to compromise.⁶⁹³ However, this action is related only to the enforcement of such matters and not all interest is prohibited save for *Riba* under its definition (see Chapter Four).

Thus, under the nature of arbitration under *Sharia* law, all commercial contracts such as loan contracts are subject to compromise and to arbitration from the *fortiori* (see Chapter One). In addition, *Sharia* allows disputes related to commercial matters to be submitted to arbitration and should be arbitrable under the enforcement the arbitration agreement stage (see Chapters Two and Four). In Saudi law, criminal and personal status disputes are not arbitrable,⁶⁹⁴ but disputes related to commercial matters are generally arbitrable.⁶⁹⁵ However, it has been suggested that in order to comply with international practices, the Saudi court shall not review a dispute that is submitted to arbitration if the arbitration agreement exists⁶⁹⁶ and the matter may only be

⁶⁸⁷ Albert Jan van den Berg, 'Yearbook Commercial Arbitration' [2004] Kluwer Law International 965; Zekos 61; Carbonneau. 'Revolution in Law through Arbitration, The Eighty- Fourth Cleveland-Marshall Fund Visiting Scholar Lecture' 239–65. See *Tricon Energy Limited v. Vinmar International, Ltd.*; see *Party Yards, Inc v Templeton BT - So 2d* (2000) 751 121. "held that a usury violation is not arbitrable; it is a matter for the courts"; Karen Halverson Cross, 'Letting the Arbitrator Decide Unconscionability Challenges' (2011) 26 *The John Marshall Institutional Repository* <<http://repository.jmls.edu/cgi/viewcontent.cgi?article=1350&context=facpubs>> accessed 9 October 2015.

⁶⁸⁸ See *Pang v. INTERNATIONAL DOCUMENT SERVICES BT - UT* [28].

⁶⁸⁹ *Hayes v. County Bank*, 713 N.Y.S.2d 267 (N.Y. Sup. Ct. 2000) 'held that the FAA permits setting aside arbitration agreements on unconscionability grounds, and a payday loan scheme with such a contract was found to be unconscionable'; *Party Yards, Inc. v. Templeton*, 751 So. 2d 121 (Fla. Dist. Ct. App. 2000) 'held that a usury violation is not arbitrable; it is a matter for the courts'.

⁶⁹⁰ Act (2) of the Saudi Arbitration Law 2012 "Without prejudice to provisions of Islamic Sharia and international conventions to which the Kingdom is a party", the same legal effect in 238 of UAE civil Law and 1 of Egyptian Arbitration Law, without Sharia term.

⁶⁹¹ See Act (2) of the Saudi Arbitration Law 2012 "shall not apply to personal status disputes or matters not subject to reconciliation".

⁶⁹² Omar M Aljazy, 'Arbitrability In Islamic Law' (2000) 12 *The Lebanese Review Of Arbitration* 348.

⁶⁹³ See Ahdab and El-Ahdab 15; see also Omar M Aljazy, 'Arbitrability In Islamic Law' (2000) 12 *The Lebanese Review Of Arbitration* 348.

⁶⁹⁴ See Act (2) of Saudi Arabia's Enforcement Law, issued through Royal Decree No. M/53 of July 3, 2012

⁶⁹⁵ Art 2, 3 and 8 of Saudi Arbitration Law where refer to commercial disputes.

⁶⁹⁶ Art 11 of the Saudi Arbitration Law.

considered by the arbitral tribunal. The arbitral tribunal has jurisdiction to consider the scope of arbitration and the validity of such agreement.⁶⁹⁷ Egyptian Arbitration law is similar to Saudi Arbitration Law in some provisions.⁶⁹⁸ However, Egyptian law is more clear with regards to the “arbitrable” question, which may include banking, investment contracts and most contracts⁶⁹⁹ that may be linked to interest.

In UAE, however, arbitration is possible where compromise is possible, and any dispute with regards to enforcement of a particular contract may be arbitrated,⁷⁰⁰ but the case is completely different due to the confusion in its law. In UAE the compromise or settlement of any dispute must relate to permissible subject matters for contracts and not contradict mandatory law or UAE public policy.⁷⁰¹ In addition, ‘the Court of Cassation has on many occasions determined that as a matter of UAE law no conciliation is permitted for matters relating to public policy’.⁷⁰² In contrast, the UAE civil code refers to some matters that can be settled or lawful to enter into a compromise, as following;

[T]he annulment of a debt by another debt, the sale of food by way of commutative contract prior to delivery, the deferred exchange of gold against silver and vice versa, usurious interest in consideration of the deferment of the payment of a debt and substituting part of a deferred debt owed by a debtor in consideration of advancing the date of payment; and a loan involving interest.⁷⁰³

It means these matters are not eligible for settlement by arbitration and that usury or interest-based loans or debt is non-arbitrable. Paying an interest-based loan is allowed under the civil code of UAE, likewise the situation in Egypt (see Chapter Three).⁷⁰⁴ Such confusion is a reflection of misinterpretation and having adopted both *Sharia* law and Civil Law (see Chapter Three). To clarify, non-arbitrable matters are limited to civil loans, where interest-based civil loans are considered usury according to the interpretation of a UAE court (see Chapters Three and Four). However, there are those who believe it is not clear whether compound interest is

⁶⁹⁷ Art 20 of the Saudi Arbitration Law. Likewise, the principle No. XIII.2.4 (a) of Trans-Lex.

⁶⁹⁸ See Gemmell (n 114)187. See Arts (1) and (11) the Egyptian Arbitration Law.

⁶⁹⁹ Act (2) of the Egyptian Arbitration Law. But, the fundamentals matters related to the economy, social life, politics, and morals, or domestic public policy may affect the enforceability under the Egyptian law.

⁷⁰⁰ In Act 203 (1) and (4) of the Civil Procedure Code of UAE, see (UAE Federal Law No. 11 of 1992 as amended)

⁷⁰¹ Art 725 of the UAE Federal Law No. 5 of 1985

⁷⁰² See Fiona Campbell, ‘Arbitrability of Disputes: Issues of Arbitrability and Public Policy in the UAE’ (*Al Tamimi & Company*, 2014) <<http://www.tamimi.com/en/magazine/law-update/section-8/may-7/arbitrability-of-disputes-issues-of-arbitrability-and-public-policy-in-the-uac.html>> accessed 10 October 2015. ‘Arbitrations in the UAE are governed by the provisions found in Chapter 3 of the Civil Procedures Law (Federal Law No. 11 of 1992)’.

⁷⁰³ See Karim Nassif, ‘Arbitrability Under UAE Law’ in Jalal El-Ahdab (ed), *International Journal of Arab Arbitration*, vol 5 (2013) 5–9; See Campbell (n 114); See also 733 of the UAE Federal Law No. 5 of 1985. That ‘Article 733 of the Civil Code states that ... usurious transactions are unequivocally not permitted to be the subject matter of an accord or compromise and are thus not arbitrable’. See Campbell (n 114).

⁷⁰⁴ Under Articles 61 and 62 of the Civil Courts Procedures Law. In Arts 76 and 77 of Federal Commercial Transactions Law, which must not exceed 12% per annum in commercial matters and 9% for non-commercial matters, Arts 76 and 77 of Federal Law 18 of 1993 that asserted provisions of Articles 61 and 62, For e.g. see *Airmech Dubai LLC v. Moxel International LLC*, Court of Cassation of Dubai, Appeal No. 132 of 2012, 18 September 2012 in Jalal El--Ahdab (ed), ‘International Journal of Arab Arbitration’ (2013) 5(1) International Journal of Arab Arbitration, 56.; See the judgment of the Federal Supreme Court of Abu Dhabi 245/20 of May 7 2000.

allowed in practice or not, or whether the courts will deem a dispute of this nature as arbitrable or not.⁷⁰⁵ The prohibition may be limited to illegal interest, compound or interest-based civil loans, and there is a distinction between individuals and companies. Whether or not the award is considered under the DIFC gives a different result.⁷⁰⁶

5.2.2 Compensation and interest in late payment

Most countries allow compensation or interest, whether for mere late payment or for actual damages under several different laws and practices (see Chapter Four). In general, these types of disputes are arbitrable, and they are considered the most common disputes of commercial transactions and contracts disputes, thereby logically such disputes would be submitted to arbitration. However, any confusion resulting from a misinterpretation would prevent arbitration from achieving its intended function.⁷⁰⁷ Interest with regards to late payment may be considered *Riba* under *Sharia* (see Chapter Four). Thus, it may be taken as same as interest-based loan under Saudi seat in some circumstances.

Most justifications for refusing the recognition and enforcement of the arbitration agreement contain matter that cannot be submitted to arbitration under the grounds of non-arbitrable are also based on the grounds of public policy.⁷⁰⁸ Such matter is related to the substantive and procedural rules of the arbitration seat the same as related to public policy. Thus, 'no public policy considerations require these claims to be handled exclusively by state courts; therefore these claims are arbitrable'.⁷⁰⁹ Logically, there is no compelling reason to not submit such types of disputes to arbitration, whatever the reasons and justifications are that all

⁷⁰⁵ See Mistelis and Brekoulakis 293–316. "Given the express statement of the Law and the Interpretative Decision No. 14/9 (28 June 1981) of the Constitutional Department of the Federal Supreme Court of Abu Dhabi (economic necessity requires the charging of simple interest by banks), as well as Judgment No. 245/20 (7 May 2000) of the Federal Supreme Court of Abu Dhabi (equally endorsing simple interest), disputes as to simple interest must be presumed as arbitrable in the UAE". See also Hind Tamini, 'Interest under the UAE Law and as Applied by the Courts of Abu Dhabi' (2002) 17 Arab Law Quarterly p50, 50; Gordon Blanke and Celine Abi Habib Kanakri, 'Arbitration in Dubai: A Basic Primer' in Christian Klausegger and others (eds), *Austrian Yearbook on International Arbitration 2011* (Manz'sche Verlags- und Universitätsbuchhandlung 2011) 217–255.

⁷⁰⁶ 'Prohibition on agreeing to usurious interest in any type of civil or commercial transaction under Article 409 of the Penal Law and Article 714 of the Civil Transactions Law is limited to transactions between individuals without extending to transactions between individuals and corporate entities which can agree with other corporate entities or individuals on conventional interest. As per the documents, the parties to the agreement subject of dispute in question are corporate entities; therefore any interest awarded is permissible'. See Hassan Arab and Marwa El Mahdy, 'DUBAI CASSATION COURT EMPHASISES ITS STRICT COMPLIANCE TO THE NEW YORK CONVENTION' (*Al Tamimi & Company*, 2013) <<http://www.tamimi.com/en/magazine/law-update/section-5/february-4/dubai-cassation-court-emphasises-its-strict-compliance-to-the-new-york-convention.html>> accessed 1 March 2016.

⁷⁰⁷ In some cases, the misinterpretation leads the confusion, in *Higher Regional Court of Munich, decision - SchiedsVZ*, where the French party has interpreted the breach of contract as a tort in attempt to avoid the arbitration where stated that such matter is non-arbitrable under the French law.

⁷⁰⁸ See e.g. Born 2015, 6, 606, 3786 'cases where a court in the arbitral seat decides that a dispute is nonarbitrable or that the arbitration agreement violates local public policies, present special issues.'; See e.g. Chernick, Kolkey and Neal 113,945; see also Mistelis and Brekoulakis 169, 285, 341.

⁷⁰⁹ Mistelis and Brekoulakis 169.

commercial disputes can be settled by arbitration,⁷¹⁰ except if unfair or unreasonable terms are related to the contract, which would be non-enforceable and may affect the arbitration agreement. However, this differs among jurisdictions.

Bankruptcy may be considered as non-arbitrable, or may affect an arbitration agreement.⁷¹¹ Bankruptcy here is related to late payment, where such late payment would be the result of the bankruptcy. In principle, bankruptcy matters are different under some circumstances, such as the applicable law and public policy.⁷¹² Bankruptcy matters should be considered as arbitrable regardless of the place that the bankruptcy occurred. However, for the favour of arbitration the court should first enforce the arbitration agreement and refer the dispute to the arbitration tribunal, who applies the law that has been chosen by the parties or else the relative applicable law.⁷¹³

⁷¹⁰ See e.g. *Parsons & Wh. Ov. Co., Inc. v. Societe G. De L. Du P.(R.)*, 508 F.2d 969 (2d Cir. 1974) at 975 'The mere fact that an issue of national interest may incidentally figure into the resolution of a breach of contract claim does not make the dispute not arbitrable.'. see sections 48 and 49 of the Arbitration Act 1996, see Chapter Four.

⁷¹¹ See 'Syska & Elektrim SA v. Vivendi & Others, Elektrim, a Polish company, entered into an agreement with Vivendi containing an agreement to arbitrate in London. After Vivendi commenced arbitration proceedings against Elektrim, the latter was declared insolvent. The question was whether the Polish Bankruptcy and Reorganisation Law, the application of which would annul the arbitration agreement, was relevant to determine the arbitrability of the dispute.' See Mistelis and Brekoulakis 116. Where it affects the capacity of the party therefore affect the validity of the arbitral agreement. However, 'even in arbitration-friendly jurisdictions, it remains the position that...matters, and those which affect the capacity or legal status of a person (individual or corporate) including bankruptcy or insolvency, are usually not arbitrable'. see Campbell. In France, matters such as bankruptcy is non arbitrable, because it relates to a third party. Born (n 22) 961; Thomas E Carbonneau, *Toward a New Federal Law on Arbitration* (Oxford University Press 2014) 45; Savage and Gaillard 330; Zekos 342; Thomas E Carbonneau, *Toward a New Federal Law on Arbitration* (Oxford University Press 2014) 45; Savage and Gaillard 330. Although that the bankruptcy is not really affect the third party directly. Vorburger 35–82. However, that 'some aspects of bankruptcy procedure also continue to be inarbitrable'. See also Born 2015, 961. Fouchard observes that the bankruptcy matters are arbitrable in France but it may be set-aside if it is contrary to the public policy. see See Savage and Gaillard 342–44; Born (n 22) 997. The matters related to public policy and some matters related pecuniary value or matters related to third party are non-arbitrable under some jurisdiction such as France. Chernick, Kolkey and Neal 113; Mistelis and Brekoulakis 32, 40, 116–224; Savage and Gaillard 330; Zekos 300. The bankruptcy question varies in different countries, but the majority of contractual disputes against the bankrupt debtor are arbitrable. Lew, Mistelis and Kröll, *Comparative International Commercial Arbitration* 206–207; Simon Vorburger, 'International Arbitration and Cross-Border Insolvency: Comparative Perspectives, International Arbitration Law Library' (2014) 31 Kluwer Law International pp. 35, 99; Savage and Gaillard 355; Antoine Kirry, 'Arbitrability: Current Trends in Europe, Arbitration International' (1996) 12 *The Journal of the London Court of International Arbitration* 373, 373; Mistelis and Brekoulakis. El-Ahdab observes that the bankruptcy matter is arbitrable in the Islamic countries jurisdiction, but affect the agreement to arbitration. Indeed, the law applicable to the contract also governs the bankruptcy matter. El-Ahdab and El-Ahdab 29.

⁷¹² Vorburger 35–82; Savage and Gaillard 344–56. In addition, it is different whether the company is creditor or debtor under the French law. See National Report for France (2013). It seems they just concern the place of the occurrence of bankruptcy, not the matter of bankruptcy itself. However, with regards to bankruptcy 'established that the conflict-of-law rules and the legal concepts applicable at the seat do not automatically apply to an arbitral tribunal'. Likewise, in U.S, where the bankruptcy is subject to the bankruptcy court where it is considered non-arbitrable, while in England it is considered arbitrable under Common Law in some aspects. Such countries ignore the arbitration agreement where the courts intervene in the arbitration in all stages. In Egypt, for example the party cannot conclude the arbitration agreement before the approval from the bankruptcy court in some cases.

⁷¹³ where the law applicable to this matter varies from one country to another. See Vorburger 35–82; see also Born (n 22) 998; see *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989) See e.g. *Re American Exp Financial Advisors Securities BT - F* 3d (2011) 672 113. [140]; In re *Payton Constr Corp BT - BR* (2009) 399 352; see *Manufacturers and Traders Trust Company V. Minuteman Spill Response, INC.*, No. 3: 14-mc-18 (W.D. Pa. Aug. 31, 2015).

Thus, 'the consent of the parties that an arbitral reference is limited to matters that are arbitrable [although] most matters can and could be arbitrated'.⁷¹⁴ In general, all disputes including interest, whether there is a bankruptcy or not, are governed by the applicable law to the contract and the dispute. The result is that the intervention of the arbitration seat in the arbitration agreement leads to conflict, where in some cases it is considered such a matter is non-arbitrable, or that it is contrary to public policy,⁷¹⁵ or that the arbitral award which contains bankruptcy may be set aside under the pretext of the law governing the bankruptcy under the seat, as discussed above. However, there is confusion in the relation between the violation of public policy and the non-arbitrable, where there is no distinction between these concepts.⁷¹⁶

5.2.3 *The most influential place in arbitration*

Arbitrable matters with regards to disputes containing interest vary from one country to another according to its interpretation and the influences of some perceptions. It is necessary to differentiate between arbitration as a mechanism to resolve disputes and judicial procedures, and between enforcement of the arbitral agreement and award. The arbitration agreement is a separate contract, thereby it reflects and is subject to the desire of the parties for referral to the arbitration, even when the referral disputes included are usury, interest or any other disputes that fall within commercial matters. Thus, the existence of a valid arbitration agreement is sufficient to submit the dispute to arbitration according the type of the merit of dispute.

However, in international commercial arbitration, according to the nature of arbitration such disputes would fall within private international law, thereby being subject to freedom of the parties. In addition, all jurisdictions generally allow arbitration on commercial matters. The referral to arbitration is subject to private international law under the nature of arbitration and the principles of good faith and *pacta sunt servanda* (see Chapter Four). The Contracting State cannot invoke its own law in order to avoid arbitration or to limit the freedom of parties in this stage, in case the dispute is clearly non-arbitrable. Any restrictions that rely on non-arbitrable should only be applied in cases where there is a well-established consensus, shared by a large majority of the Contracting States, with respect to arbitration in certain matters. The existence of disputes that include interest does not mean that the issues are to be considered by the courts under the seat of arbitration.

The referral to arbitration cannot be refused due to the 'essence of the dispute' without review of the contents of the matter of the dispute, which cannot be known until a decision is reached by the arbitrator. In the enforcement stage, the arbitrable is determined under the

⁷¹⁴ Mistelis and Brekoulakis 8.

⁷¹⁵ Kirry 373.

⁷¹⁶ Born (n 22) 911; Chernick, Kolkey and Neal 113; Savage and Gaillard 344.

arbitration seat either under the applicable law to the arbitration agreement or under the law of the arbitration seat according to the Art II (1) of NYC and the type of the dispute under the parties' agreement. However, the law of the enforcement place expressly gives effect to the issue of "arbitrable" under Art V (2) (a) of the NYC.

Thus, commercial matters are arbitrable and courts should not intervene to achieve compatibility and standardization of laws in the enforcement of foreign arbitral awards according to the NYC. The arbitrators have power to consider these types of disputes unless they are expressly non-arbitrable by law. Since the agreement exists and is valid, there is nothing prevent the arbitrators to consider such disputes. In general, it seems that the referral of disputes containing interest etc. to arbitration are arbitrable, logically, as long as there was an agreement. However, it remains a problem, where one would note that such interpretation may not be followed under Article V (2) (a) of NYC where Art II (1) remains with regards to the governing the arbitrable. In that situation at hand, there may be a conflict between the applicable law to the arbitration agreement, and the law of the seat of arbitration. Consequently, the answer has to be found from the arbitration agreement law.

Art II (1) refers "*Each Contracting State shall recognize an agreement*". It refers to disputes that may occur any time from the words '*all or any differences which have arisen or which may arise*', where it is difficult to determine the type of matter of dispute, especially with regards to disputes that may arise. In brief, non-arbitrable considerations would lead to possible invalidity of the arbitration agreement on the part of the disputes. The existence of such an agreement means nothing in this case under these considerations, unless matters that are internationally agreed upon can never be eligible for settlement by arbitration. Mistelis and Brekoulakis stated that 'no dispute is barred from resolution by arbitration... even the fundamental question of whether a dispute falls under the exclusive jurisdiction of a judicial body may itself be arbitrable'.⁷¹⁷ According to Mistelis and Brekoulakis 'the issue of what disputes are arbitrable has now become less of a problem, some basic misconceptions about the subject of arbitrability still persist'.⁷¹⁸

⁷¹⁷ Mistelis and Brekoulakis the overview page.

⁷¹⁸ See Mistelis and Brekoulakis 19; Savage and Gaillard 995 'a dispute to be found non-arbitrable under a country's domestic law, without necessarily preventing the recognition in that country of a foreign award dealing with the same subject matter'; Sanders, *ICCA's Guide to the Interpretation of the 1958 New York Convention: A Handbook for Judges* "Each State indeed decides which matters may or may not be resolved by arbitration in accordance with its own political, social, and economic policy. Classic examples include domestic relations (divorces, paternity disputes...), criminal offences, labour or employment claims, bankruptcy, etc. However, the domain of non-arbitrable matters has considerably shrunk over time as a consequence of the growing acceptance of arbitration. It is now not exceptional for certain aspects of employment claims or claims relating to a bankruptcy to be arbitrable. Moreover, many leading jurisdictions recognize a distinction between purely domestic arbitrations and those that are of an international nature, and allow a broader scope of arbitrability with respect to the latter.".

In *Sharia* for example, a contract that contains *Riba* is unenforceable; such influence is accorded only in the stage of the enforcement of an arbitral award containing *Riba*, but it is not in the enforcement of the arbitration agreement stage. However, if the parties select *Sharia* law as a law governing the contract, the arbitrators can use *Ijtihad* and *Qiyas* to study the "il'lah" of the new case under the basic principles of Islamic contract in *Sharia* law. The arbitrators have power to decide matters under *Sharia* law, considering each case separately, as not all interest should be deemed *Riba* (see Chapters Two and Four). The approach of allowing such matters to be submitted to arbitration relies on party autonomy and the nature of arbitration. However, there is nothing preventing the referral of disputes to arbitration, whatever the merits of the dispute, in particular for disputes of commercial aspect.

5.3 The enforcement of the arbitral agreement; Non-arbitrability issues

Some issues on arbitrability demand more analysis, such as precisely determining the validity of the arbitration agreement, the authority of the arbitrator, and whether disputes have arisen or may arise are considered within the scope of the jurisdiction of the arbitrator or not. Some matters would give indirect effect to the arbitrability under the invalidity of the arbitration agreement, the incapacity of the parties under Art II of the NYC. The arbitration agreement would be invalid or voidable when it loses ground on the basis of procedural or substantive rules, or both.

Act V(1) (a) of the NYC refers to Act II. Thus, Act II gives some rules for the question of arbitrability which can be taken in advance and considered by the arbitrator. A court is compelled to refer the parties' dispute to arbitration, provided that the conditions of Art II (3) are met.⁷¹⁹ It should be noted these rules are subject to the applicable law to the agreement as mentioned earlier, and the scope of the dispute may be determined by the agreement of the parties.⁷²⁰ However, the question remains whether the arbitrators are allowed to apply a law that has not been chosen by the parties or award a rate and period of interest that the parties have not mentioned, thereby the situation may be considered indirect non-arbitrability due to the award being beyond the scope of the arbitration agreement under Art V(1) (a) of NYC.⁷²¹ Therefore, the

⁷¹⁹ Sanders (n 574) 61.

⁷²⁰ Art V (1) (c) of NYC (c) *The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced; or*

⁷²¹ Because in some cases that if the party claimed the illegal interest, the dispute will be considered as non arbitrable and if he did not specify, the dispute will be considered as outside the scope of the arbitration agreement. Some might think that such matter is limited to a particular State or a legal system, but the confusion exists in all in either the type of dispute, the applicable law, the scope of agreement, the arbitrator's authority or freedom of the parties. Arbitrable with respect to interest or usury logically is different in case whether the parties refer to these issues in their contract/agreement or not. In event that the contract contains interest or usury whether this give effect to the validity of the arbitration clause or not.

convention must be interpreted to allow redress of certain issues that are non-arbitrable, and must consider non-arbitrability with restraint rather than as a means to escape recognition and enforcement.⁷²² The NYC aims to avoid conflicts with regards to the recognition and enforcement of arbitration agreements and foreign arbitral awards as the matter of arbitrability is one of most complicated in regards to exclusive jurisdiction.⁷²³

Specifically, matters related to arbitrability with respect to disputes containing interest may affect the validity of the arbitration agreement. In the case that the contract involves interest clauses but the arbitration agreement has not referred to such dispute, the consideration of this dispute would be beyond the scope of referral to arbitration and vice versa.⁷²⁴ In case the contract does not include terms with regard to interest, but the arbitration agreement has mentioned such terms or interest disputes, it would be considered that the arbitrators have the mandate to settle such disputes. The scope of the dispute would be determined by the arbitration agreement or the terms of contract. The question remains as to whether the law chosen by the parties or by the law of arbitral seat shall determine the issue of non-arbitrability.

5.3.1 *Incapacity caused by bankruptcy*

As stated, the issue of interest may occur in disputes arising from bankruptcy which may be related to the issue of incapacity. Most national arbitration laws would reject enforcing either the arbitration agreement or the arbitral award if ‘one of the parties lacked the capacity to conclude a binding arbitration agreement’.⁷²⁵ The matter of incapacity is one that would affect the validity of the arbitration agreement as stated in Article V(1)(a) of the NYC and the Model Law.⁷²⁶ Articles 34(2)(a)(i) and 36(1)(a)(i) of the Model Law allow that an arbitral award under the arbitration agreement can be set aside or subject to non-recognition and non-enforcement if:

‘a party to the arbitration agreement...was under some incapacity; or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made’.

The Model Law with respect to the lack of capacity reflects the same principles with regards to the invalidity of the arbitration agreement. Art 34(2)(a)(i) also provides that the parties’ capacity is to be determined by the law ‘applicable to them,’ or their ‘personal law,’ again reflecting generally applicable choice of law principles. All national arbitration laws allow for the rejection of the award if ‘one of the parties lacked the capacity to conclude a binding arbitration

⁷²² Born 2015, 614–616.

⁷²³ Whether the arbitrability should be determined by court or by arbitrator.

⁷²⁴ Where a conflict has occurred because of the interest rates and the arbitration agreement scope see the case of *Tricon Energy Limited v. Vinmar International, Ltd.*

⁷²⁵ Born (n 22) 3203–04.

⁷²⁶ Eilionoir Flynn and Anna Arstein-Kerslake, ‘Support Model of Legal Capacity: Fact, Fiction, or Fantasy. The’ (2014) 32 Berkeley J. Int’l L. 124.

agreement'.⁷²⁷ In arbitration, the invalidity of the arbitration agreement is influential in its enforcement, whether because of procedural or substantive rules or simply the incapacity of the parties by bankruptcy or insolvency. It is supposed that the validity of the arbitration agreement can be determined at the stage of recognition and enforcement of the arbitration agreement by the applicable law, before the stage of recognition and enforcement of the arbitral award. If it is necessary, the review should be of the arbitration agreement itself at the recognition stage before it is binding, and before it extends to the arbitral award. In international arbitration, the arbitration tribunal or arbitrators should have the power to determine the validity of the arbitration agreement to consider the dispute, where it is not likely that a court ultimately would decide that the arbitration agreement is invalid.

An arbitration agreement would be invalidated under some national bankruptcy laws with regards to bankrupt parties.⁷²⁸ Berg observes that disputes including bankruptcy have remained in the courts and the bankrupt party cannot agree to submit to arbitration disputes arising after the order of bankruptcy is made as a matter of non-arbitrability due to incapacity according to the NYC.⁷²⁹ Bankruptcy orders lead the issue of incapacity in the context of Art V(1)(a) to be interpreted in the sense of "lacking the power to contract".⁷³⁰ Bankruptcy and capacity vary under different jurisdictions with regards to non-arbitrability.⁷³¹ In principle, 'a party in bankruptcy is prevented from arbitrating if the relevant bankruptcy law provides for such effect'.⁷³²

There should be a distinction between the questions of bankruptcy as a non-arbitrable matter and as a matter affecting capacity. According to Born 'distinction that applies to rules of substantive validity and non-arbitrability must also be drawn between rules regarding capacity and non-arbitrability'.⁷³³ The law governing capacity varies in different jurisdictions,⁷³⁴ however, the key issue is whether bankruptcy occurred before or after entering into the main contract or the

⁷²⁷ Born (n 22) 3163–3393.

⁷²⁸ Born (n 22) 894–895.

⁷²⁹ See Albert Jan van den Berg, 'Final Award in ICC Case No. 16015', *Yearbook Commercial Arbitration 2013 - Volume XXXVIII* (Kluwer Law International 2013) <http://www.kluwerarbitration.com/CommonUI/book-toc.aspx?book=TOC_ICCAYB_2013>; Berg, 'ICCA Congress Series, 1998 Paris'; see also Vorbürger 35–82.

⁷³⁰ see Flynn and Arstein-Kerslake 124 'claims relating to a bankruptcy, the term "incapacity" in the context of Article V (1)(a) is interpreted in the sense of lacking the power to contract'; see also Vorbürger.

⁷³¹ Born (n 15) 994–1007; 'UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment and Interpretation' (2014) <<http://www.uncitral.org/uncitral/publications/publications.html>>; BURTON W' WLAND, V' ROBERTA SCHNEIDERMAN, ROBERT ZIMELIS (2015) 14-11203.

⁷³² Frank Spoorenberg and Daniela Franchini, 'Bankruptcy No Restriction to Arbitration Unless It Excludes Bankrupt's Legal Capacity' (*ILO*, 2012) <<http://www.internationallawoffice.com/newsletters/detail.aspx?g=4caa30c6-e0cb-46f8-8878-fd97189e2014>> accessed 29 September 2015.

⁷³³ Born 949.

⁷³⁴ Born 3203 'In many civil law systems, the capacity of juridical persons is governed by the law of the seat of the entity in question, while in common law jurisdictions the law of the place of incorporation ordinarily applies to issues of capacity. Similarly, the capacity of natural persons in civil law jurisdictions is generally governed by the law of their nationality, while the capacity of natural persons in common law jurisdictions is governed by the law of their domicile.'

arbitration agreement. In case bankruptcy occurred after the agreement to arbitration, then such bankruptcy does not affect the capacity of the bankrupt parties.⁷³⁵

The validity of the arbitration agreement may be affected by the incapacity of the parties. The capacity of the parties shall be subject to the applicable law and it should not be considered as non-arbitrability if the incapacity was declared after the conclusion of the arbitration agreement.⁷³⁶ The arbitrator should determine both the capacity of the parties and the validity of the contract under the applicable law.⁷³⁷ Thus, the capacity of the parties can be determined before the arbitration proceedings and before such effect extends to the arbitral award. However, Born believes bankruptcy 'should not generally have effects on the validity of international arbitration agreements'.⁷³⁸

5.3.2 *The validity of arbitration agreements*

An agreement is invalid or voidable when it has failed to fulfil either or both the procedural or substantive requirements as stipulated in the NYC, the Model Law, and other national arbitration laws. Art 8 (1) of the Model Law refers the same legal action as Arts II (1) and (3) of the NYC, as do Art 7 of the Model Law and Art II (2) of the Convention. It does not mention the choice of law, but Art 8 (2) of the Model Law⁷³⁹ states that 'arbitral proceedings may nevertheless be commenced or continued, and an award may be made, while the issue is pending before the court'⁷⁴⁰, leading to more problems such as an unnecessary delay if the arbitration agreement will be considered invalid after these procedures, or else as inconsistency within the nature of arbitration.

The confusion remains in Art II (3) and Art V(1) (a) of the NYC, where Art II (3) refers to the Contracting States' obligation to recognise and enforce the arbitration agreement, while Art

⁷³⁵ Ahdab and El-El-Ahdab 29. " However, if the bankrupt signed an arbitration agreement before bankruptcy proceedings were initiated, the agreement would be valid and binding upon the bankruptcy trustee.... Consequently, arbitration is possible concerning the monetary aspects of bankruptcy."; See Art 10 (1) of the Saudi Arbitration Law 2012 that the arbitration agreement would be valid only in event it was concluded by parties having legal capacity to dispose of their rights. Ahdab and El-El-Ahdab 29 'However, if the bankrupt signed an arbitration agreement before bankruptcy proceedings were initiated, the agreement would be valid and binding upon the bankruptcy trustee.... Consequently, arbitration is possible concerning the monetary aspects of bankruptcy.'; See Art 10 (1) of the Saudi Arbitration Law 2012 that the arbitration agreement would be valid only in event it was concluded by parties having legal capacity to dispose of their rights.

⁷³⁶ See Zekos 343 ' simply with the question of whether the relevant person has the legal capacity to dispose of its property or rights. It has to be decided firstly whether the subject matter of a dispute is arbitrable and only then is it necessary to enquire whether the person has legal capacity to enter into an arbitration agreement relating thereto. This author thinks that the legal capacity of person to conclude arbitration agreements should not be considered as a matter of arbitrability'; see also Born 440,994–998,1060..

⁷³⁷ There who observes that the arbitrators cannot decide the legal capacity of the parties, see Anders Forss, 'Arbitration in Finland - Lexology Navigator Q&A' (*Association of Corporate Counsel*, 2014) <<http://www.lexology.com/library/detail.aspx?g=705397b6-425b-4a7a-85a7-965e3996c060>> accessed 10 October 2015.

⁷³⁸ Born (n 22) 895.

⁷³⁹ Born 479.

⁷⁴⁰ Art 8 (2) of the UNCITRAL Model Law.

V(1) (a) refers to the grounds for refusal of enforcement of the arbitral award due to invalidity of the arbitration agreement or incapacity of parties. Art II (3) refers to any matters that can affect the validity of the arbitration agreement such as fraud or if such agreement was unwritten etc. National courts or the arbitrator should consider the applicable law to the arbitration agreement in the first stage under the rules of Art V(1) (a) of the NYC in order to avoid duplicate reviews in the enforcement stage of the arbitral award. In case the arbitrators determine the validity of the arbitration agreement, including the capacity of the parties under the applicable law, under the Art II (3) of NYC, such action thereby would lead to avoiding legal action of the Art V(1) (a) of NYC.

5.3.2.1.1 The law determines the validity of the arbitration agreement

In general, the law applicable to the arbitration agreement determines the validity of the arbitration agreement, whether procedural or substantive (see Chapter Three). Mistelis and Brekoulakis observe that 'the arbitral tribunal will decide the issue of arbitrability by application of the law that governs the arbitration agreement, irrespective of the principle of separability (severability), being, often, the law that governs the main contract.'⁷⁴¹ However, they also observe that '*Lex arbitri*: arguably the law applicable to an arbitration agreement, it is the source of power of the arbitrator' or '*Lex contractus – lex causae*: only to the extent that the law applicable to an arbitration agreement has not been determined'.⁷⁴² Regardless, the applicable law to the arbitration agreement determines the validity of such agreement (see Chapter Three). In addition, the applicable law to the contract is the law that determines the validity of such contract. These may be the same law in some cases.

The law of the seat of arbitration or the law of the enforcement place may also affect the determination of the applicable law to the arbitration agreement if it is considered by the courts. For example, the Saudi Arbitration law emphasizes that the arbitration agreement is enforced unless it is inconsistent with *Sharia*,⁷⁴³ and the law governing the arbitration agreement shall not be contrary to *Sharia*. It is not necessarily the case that the arbitration agreement or the chosen foreign law governs that the arbitration agreement is contrary to *Sharia* law (see Chapter Two). Similar logic can be observed in the English practice where the law governs the arbitration agreement shall not be contrary to the mandatory provision under an English seat.⁷⁴⁴ (see Chapter

⁷⁴¹ Mistelis and Brekoulakis 136.

⁷⁴² Mistelis and Brekoulakis 136.

⁷⁴³ Act (2) and (5) of the Saudi Arbitration Law, the same legal effect in 238 of UAE civil Law and 1 of Egyptian Arbitration Law, without referring to *Sharia*.

⁷⁴⁴ In the case of *Arsanovia Ltd, Burley Holdings Ltd and Unitech Ltd v Cruz City 1 Mauritius Holdings*, [2012] EWHC 3702 (Comm), "The difficulty that arises here and has arisen before is that the parties have chosen as the *lex causae* the law of one country, but by agreeing to resolve disputes through arbitrations with a seat elsewhere they have clearly indicated the choice of a different *lex fori*. In these circumstances, which law is (or, notionally, laws are) applicable to the arbitration agreement and determines the jurisdiction of a tribunal appointed under it? More

Three). In the U.S., courts intervene in the arbitration agreement and the chosen law.⁷⁴⁵ The law of the court may be applied in most cases, especially where there is no jurisdiction for the arbitrator in determining the validity of the arbitration agreement. In France, the courts have developed an innovative doctrine where arbitration agreements are autonomous from national law and instead are subject to specific principles of international law.⁷⁴⁶ Thus, under the parties' autonomy, the law applicable to the arbitration agreement should not be affected, and the arbitrator should determine the applicable law to the arbitration agreement and therefore the validity of such agreement. However, the provisions of Art V are applicable only in the judicial enforcement forum, without broader effect on courts in other Contracting States.⁷⁴⁷

5.4 The enforceability of the arbitral award under Art V(1)(a) of the NYC

The arbitral award would be non-enforceable under the request of a party if the agreement was invalid.⁷⁴⁸ Additionally, the same legal action applies if the dispute was not covered by the arbitration agreement or was settled beyond the scope of such agreement.⁷⁴⁹ Determining the rate and period of interest by the arbitrators may be considered beyond the scope of agreement of the parties. The scope of the dispute in arbitration may be determined by the arbitration agreement or by the contract terms. Such matter would be different whether the parties have agreed to the law and terms or leave the determination to the arbitrators, and whether the dispute has already arisen or will arise.

5.4.1 *The validity of the underlying contract*

Art V (1) (a) of the NYC refers implicitly to the validity of the main contract and its effect on the validity of the arbitration agreement. In the U.S., under the FAA, the arbitration agreement and the contract 'shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract'.⁷⁵⁰ However, the arbitration agreement may be invalidated or set aside in the event the contract is questioned.⁷⁵¹ The task of determining arbitrability belongs to the tribunal in the first instance, then the court under its law, and not the

specifically, here the *lex causae* of the SIA is (by the parties' express choice) the law of India whereas the seat of the arbitration is (by the parties' express choice) London and so the curial law of the arbitration is English. Which of these two candidates is applicable to the arbitration agreement?"

⁷⁴⁵ Born 986.

⁷⁴⁶ Born, *International Arbitration: Cases and Materials* 65.

⁷⁴⁷ Born (n 22) 613 'Importantly, unlike the generally-applicable choice-of-law and contractual validity rules under Article V (1)(a), Article V (2)(a)'s non-arbitrability provision is an exception, applicable only in the judicial enforcement forum, without broader effect on courts in other Contracting States – which remain bound by Article V (1)(a)'s choice-of-law regime.'

⁷⁴⁸ Under Art V (1) (a) of the NYC

⁷⁴⁹ Under Art V (1) (c) of the NYC

⁷⁵⁰ Section 2 of the Federal Arbitration Act.

⁷⁵¹ See *Pang v. International Document Services BT - UT* [28]; see also *Hayes v. County Bank*, 713 N.Y.S.2d 267 (N.Y. Sup. Ct. 2000) 'held that the FAA permits setting aside arbitration agreements on unconscionability grounds, and a payday loan scheme with such a contract was found to be unconscionable'.

law chosen by the parties⁷⁵² unless the parties clearly provided otherwise.⁷⁵³ In England, where the main contract fails or is said to be invalid does not mean the arbitration agreement automatically also fails or becomes invalid.⁷⁵⁴ The courts determine arbitrability on a case-by-case basis.⁷⁵⁵ English courts may reject enforcing the award and invalidate the arbitration agreement regarding an illegal contract under public policy.⁷⁵⁶

The U.S. courts decide non-arbitrability issues unless the parties expressly agree that the arbitrator has jurisdiction to decide such issues. The FAA does not expressly deal with such matters as the separability doctrine, the allocation of competence between U.S. courts and arbitrators to resolve disputes over arbitration agreements.⁷⁵⁷ The courts in the U.S. consider whether the agreement to arbitration is valid or not, and sometimes it is considered by the courts and by the arbitrator at the same time.⁷⁵⁸ Hence, if the challenging party attacks the arbitration clause itself, the challenging party can seek court intervention to deem the arbitration clause invalid.⁷⁵⁹ However, for the validity of the contract in general, as opposed to the arbitration clause in particular, it is the arbitrator and not the court who decides the issue.⁷⁶⁰ The validity of the arbitration agreement should not be considered by the court, whether the challenge is to the

⁷⁵² *Becker Autoradio U.S.A., Inc. v. Becker Autoradiowerk GmbH*, 585 F.2d 39, 43 (3rd Cir. 1978) 'It is true that, if the parties agree that certain disputes will be submitted to arbitration and that the law of a particular jurisdiction will govern the resolution of those disputes, federal courts must effectuate that agreement. However, whether a particular dispute is within the class of those disputes governed by the arbitration and choice of law clause is a matter of federal law.'; *Chloe Z Fishing Co., Inc.*, 109 F. Supp. 2d at 1254.

⁷⁵³ *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 945 (U.S. S. Ct. 1995).

⁷⁵⁴ *Beijing Jianlong Heavy Industry Group v Golden Ocean Group and others* [2013] EWHC 1063 (Comm) the Commercial Court considered the validity of the arbitration clauses contained in guarantees that were unenforceable by reason of illegality.

⁷⁵⁵ Tang 94.

⁷⁵⁶ See *Lemenda Trading Co. v. African Middle East Petroleum Co.*, [1988] Q.B. 448, 456 (Comm. Ct.) (Eng.) indicating that on grounds of public policy, English courts have refused to enforce an agreement in a number of cases. In *Soleimany v. Soleimany*, [1999] Q.B. 785, 804 (C.A.) (Eng.), the Court of Appeal of England and Wales accepted the public-policy argument of the party opposing enforcement and refused to enforce the arbitral award. Sion Soleimany asked his son Abner Soleimany to return to Iran to recover some carpets that Iranian customs authorities had seized. Id. at 789. After Abner discovered that he could profit from exporting Persian carpets for sale in England, he entered into an arrangement with Sion to split the profits. Id. The exportation of these carpets constituted smuggling because it contravened Iranian revenue laws and export controls. Id. Eventually, disputes arose between Sion and Abner over the division of profits. Id. Consequently, they agreed to arbitrate their differences in front of the Beth Din, a Judaism court, with Jewish law governing the arbitration. Id. Subsequent to the arbitral award in favor of Abner, Abner attempted to enforce the award in England. Id. at 791. Sion opposed enforcement of the award on the ground that it was contrary to English public policy to enforce an award resulting from an illegal contract. Id. at 787-88. The Court of Appeal of England and Wales first addressed the separability doctrine: not all illegal contracts will infect and void an arbitration agreement, and not all arbitration agreements will be valid regardless of a valid contract. Id. at 797. Next, the court set forth the rule that "it is contrary to public policy for an English award . . . to be enforced if it is based on an English contract which was illegal when made." Id. at 799. The court reasoned that public policy would not allow parties to override the judicial process by using arbitration to hide their illegal contract. Id. at 800. Unlike the Westacre contract that the arbitrators in Westacre held that the underlying contract was not illegal. Id. at 802. however, both the arbitration panel and the court in *Soleimany* found that the contract was blatantly illegal. *Soleimany*, [1999] Q.B. at 792. Accordingly, the court refused to enforce the award as contrary to public policy. Id. at 804.

⁷⁵⁷ Born, *International Arbitration: Cases and Materials* 53.

⁷⁵⁸ In California, the case consider by the court and arbitration in the same time, See *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989) at [487]

⁷⁵⁹ *Mistelis and Brekoulakis* 70.

⁷⁶⁰ *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 409 (1967).

contract or to the arbitration clause or as a separate agreement under separability, unless it is found invalid from the beginning under the law of the arbitration seat.

5.4.1.1 Application of the principle of separability in usury case

The separability principle says that an arbitration clause is treated as separate contract from the underlying contract in which it is included. Under the principle of separability, the invalidity of the underlying contract does not automatically extend to the arbitration clause contained therein unless it is proven that the arbitration agreement itself is vitiated by fraud or does not exist.⁷⁶¹ According to Sanders, separability ensures that if the arbitrator decides the underlying contract as invalid, it 'does not saw off the legs of the chair on which it is sitting', thereby if 'the contract is null and void, shall not entail *ipso jure* the invalidity of the arbitration clause'.⁷⁶² The principle of separability reversed the practice of most courts despite the fact that there are those who do not support the principle of separability.⁷⁶³

In *Lytle v. CitiFinancial Services, Inc.*,⁷⁶⁴ a dispute over a loan contract, the Plaintiffs claimed that it 'violate[s] state and federal laws as well as Pennsylvania common law',⁷⁶⁵ and the 'ruling was error as the arbitration provisions of the loan contract are unenforceable under Pennsylvania law'.⁷⁶⁶ However, 'Pennsylvania law and federal law, as applicable ... [i]f any part is unenforceable, this will not make any other part unenforceable. In no event will Borrower be required to pay interest or charges in excess of those permitted by law'.⁷⁶⁷ The court held 'a finding that a contract is one of adhesion does not require that the court find the contract unconscionable'.⁷⁶⁸

In *Margaret O'Shea v. Direct Financial Solution, LLC*, the plaintiff filed a claim to the court of common pleas of Philadelphia, claiming that the practices by Defendants were unfair and illegal due a violation of the usury law. The plaintiff claimed that the interest rates were in excess of the maximum allowed according to Pennsylvania usury law. In addition, the plaintiff

⁷⁶¹ See the principle XIII.2.4 (c) of Trans-Lex.

⁷⁶² Pieter Sanders, *The Work of UNCITRAL on Arbitration and Conciliation* (Kluwer Law International 2004) 96.

⁷⁶³ For three main reasons; "first, separability represent a derogation of contract law. Second, rejection of separability is consistent with the policy of the FAA. Finally, the view handles the momentous waiver of access to courts in an appropriate manner". See Michelle St. Germain, 'Arbitrability of Arbitrability' (2005) 2005 *The Journal of Dispute Resolution* 523, 534.

⁷⁶⁴ *Lytle v. CitiFinancial Services, Inc.*, 810 A.2d 643 (Pa. Super. Ct. 2002).

⁷⁶⁵ *Lytle*, 810 A.2d at 647

⁷⁶⁶ *Lytle*, 810 A.2d at 648

⁷⁶⁷ *Lytle*, 810 A.2d at 649, compare to *Thibodeau v. Comcast Corp.*, 912 A.2d 874 (Pa. Super. Ct. 2006).

'Pennsylvania law concerning the enforceability of arbitration agreements is in accordance with Federal law, requiring that arbitration agreements be enforced as written and allowing an arbitration provision to be set aside only for generally recognized contracted defenses such as duress, illegality, fraud and unconscionability.', see *Thibodeau* 912 A.2d at [880]

⁷⁶⁸ *Lytle*, 810 A.2d at 658. However, 'the application of the arbitration clause would result in unfair surprise to Thibodeau. ... Under these circumstances, we agree with the trial court that the application of this arbitration clause would result in unfair surprise to the consumer.' See *Thibodeau* 912 A.2d at [887]

alleged that the procedural and substantive rules were unconscionable, unenforceable and invalid.⁷⁶⁹ The plaintiff argued that:

Under the FAA, in order to determine if there is an enforceable arbitration agreement between the parties that compels arbitration and a stay or dismissal of the present action, a court must consider: (1) whether a valid agreement to arbitrate exists between the parties and (2) whether the specific dispute falls within the substance and scope of that agreement.⁷⁷⁰

Each loan agreement includes a separate arbitration agreement and these arbitration agreements state any disputes related to these contracts should be resolved by arbitration. Borrowers should not file a claim before the court and waive their right. Additionally, the arbitrator's award with respect to any dispute is considered final and binding according to the Utah arbitration act. However, the arbitration agreements were valid because both parties entered into an agreement referring to arbitration and the plaintiff has failed to proof of damages. Thus, the court held that:

The Arbitration Agreements are valid under Pennsylvania law, because: (1) the parties entered into an agreement to arbitrate, as evidenced by the signed loan agreements; and (2) Plaintiff's claims fall within the scope of the Arbitration Agreements, which state that "all federal and state law claims" and "all common law claims, based upon contract, tort, fraud, or other intentional torts" are subject to arbitration under the Agreements. Thus, the only matter to be decided is whether the Arbitration Agreements are unconscionable and therefore invalid. Although Pennsylvania law allows a court to set aside an arbitration provision where the provision is procedurally and substantively unconscionable, Plaintiff has failed to substantiate her claims of unconscionability.⁷⁷¹

In the *Prima Paint* case,⁷⁷² the court adopted the principle of separability where the invalidity of the contract does not exceed to the validity of the arbitral agreement. The U.S. Supreme Court relied on separability in holding that arbitrators rather than courts could decide claims that a party has been fraudulently induced to enter into the main contract. However, if a contract containing an arbitration clause can be rescinded on the ground of fraud, is to be decided by the courts and not by the arbitrators.⁷⁷³ This case was the first step in the federalization of the law of arbitration and in establishing a single national law of arbitration.⁷⁷⁴ After almost forty years, in *Buckeye Check Cashing, Inc. v. Cardegna*,⁷⁷⁵ the Florida Supreme Court refused to enforce the arbitral agreement because the underlying contract was invalid and unenforceable

⁷⁶⁹ See also *Pang v. International Document Services BT - UT* [28]; see also *Hayes v. County Bank*, 713 N.Y.S.2d 267 (N.Y. Sup. Ct. 2000) 'held that the FAA permits setting aside arbitration agreements on unconscionability grounds, and a payday loan scheme with such a contract was found to be unconscionable'.

⁷⁷⁰ *Margaret O'Shea v Direct Financial Solutions, LLC, d/b/a Cash Central, Civil Action* (E.D.PA. 2007) 07-1881.

⁷⁷¹ *Margaret O'Shea v. Direct Financial Solutions, LLC, d/b/a Cash Central, Civil Action*.

⁷⁷² *Prima Paint Corp. v. Flood & Conklin Mfg. Co. BT - US*.

⁷⁷³ *Prima Paint Corp. v. Flood & Conklin Mfg. Co. BT - US* [425].

⁷⁷⁴ Carbonneau, 'Revolution in Law through Arbitration, The Eighty- Fourth Cleveland-Marshall Fund Visiting Scholar Lecture' 250.

⁷⁷⁵ *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 126 S. Ct. 1204, 163 L. Ed. 2d 1038 (2006).

rather than fraudulent. It found that the contract was contrary to the usury law. The whole contract was invalid, therefore a court and not the arbitrator should consider the dispute as is illegal and void. Thus,

The District Court of Appeal of Florida for the Fourth District reversed, holding that because respondents did not challenge the arbitration provision itself, but instead claimed that the entire contract was void, the agreement to arbitrate was enforceable, and the question of the contract's legality should go to the arbitrator.⁷⁷⁶

However, In *Prima Paint*, the Florida Supreme Court relied on the distinction between void and voidable contracts, but in *Buckeye* the Court made clear that challenges directed toward the underlying contract are "irrelevant" for severability purposes⁷⁷⁷ The Florida court distinguished *Prima Paint* on the ground that fraudulent inducement only rendered a contract voidable, while an illegality challenge, if accepted, would render the contract void from its inception. According to the court a voided contract affects and nullifies all of its provisions including the arbitration clause.⁷⁷⁸

As a matter of substantive federal arbitration law, an arbitration provision is severable from the remainder of the contract.⁷⁷⁹ The U.S. Supreme Court held '[w]e reaffirm today that, regardless of whether the challenge is brought in federal or state court, a challenge to the validity of the contract as a whole, and not specifically to the arbitration clause, must go to the arbitrator'.⁷⁸⁰ Therefore, the FAA cannot be the basis for displacing a state law that prohibits enforcement of an arbitration clause contained in a contract that is unenforceable under state law.⁷⁸¹ Under arbitrability, the Court extended *Prima Paint* in two ways, holding that (1) arbitrators can decide whether the underlying contract is illegal, such as including usury; and (2) that separability applies in a state court as well as a federal court.⁷⁸²

It is more strict under different jurisdictions, for example '[u]nder California law, courts may refuse to enforce any contract found "to have been unconscionable at the time it was made," or may "limit the application of any unconscionable clause"'.⁷⁸³ However, under California law

⁷⁷⁶ *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. at 440.

⁷⁷⁷ *Buckeye Check Cashing, Inc. v. Cardegna BT - US* 'In declining to apply *Prima Paint*'s rule of severability, the Florida Supreme Court relied on the distinction between void and voidable contracts. 'Florida public policy and contract law,' it concluded, permit 'no severable, or salvageable, parts of a contract found illegal and void under Florida law.' *Prima Paint* makes this conclusion irrelevant. That case rejected application of state severability rules to the arbitration agreement without discussing whether the challenge at issue would have rendered the contract void or voidable. So also here, we cannot accept the Florida Supreme Court's conclusion that enforceability of the arbitration agreement should turn on 'Florida public policy and contract law'.

⁷⁷⁸ *Cardegna v. Buckeye Check Cashing, Inc.*, 894 So. 2d 860, 865 (Fla. 2005) at [863].

⁷⁷⁹ *Buckeye Check Cashing*, 546 U.S. at 445-49.

⁷⁸⁰ *Buckeye Check Cashing*, 546 U.S. at 449

⁷⁸¹ *Buckeye Check Cashing*, 546 U.S. at 449

⁷⁸² *Ibid.* at 449.

⁷⁸³ *At&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 563 U.S. 321, 179 L. Ed. 2d 742 (2011) at [1746].

the doctrine of separability does not make consideration with regards to unconscionability.⁷⁸⁴ Such matter depends on whether the arbitration agreement is separate from or connected to the underlying contract as well as whether the contract contains terms violating the procedural or substantive law (see Chapter Four). Agreement on interest that violates usury law,⁷⁸⁵ include a waiver of a legal right,⁷⁸⁶ or violation of the principle of good faith,⁷⁸⁷ is considered unconscionability and leads to non-enforcement of the contract or part of it under different laws, or may affect the enforcement of the arbitration agreement.⁷⁸⁸ It should not affect the referral to arbitration and the validity of the arbitration agreement, whether it is connected or in a separate agreement form.⁷⁸⁹ The applicable law of each contract should be considered, be in the basic contract or arbitration agreement, according to related law. In *Nagrampa v MailCoups, Inc BT*, the U.S. Court of Appeals Ninth Circuit stated that the award would be rejected if the contract includes illegal interest or usury,⁷⁹⁰ however, it observed that the contract was valid under California law.⁷⁹¹

The approach in Texas is completely different from the Californian approach, for example in *Nagrampa v MailCoups, Inc BT*,⁷⁹² where in Texas the invalid contract is unenforceable under the substantive law and under public policy, while in California it is considered enforceable under the doctrine of separability. California follow such doctrine but it

⁷⁸⁴ *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* [1006] 'that the question of arbitrability was for it to decide, and we AFFIRM the district court's holding that California law applies and renders the arbitration agreement unconscionable and accordingly, unenforceable.'

⁷⁸⁵ As in buckeye

⁷⁸⁶ 'that the provision waiving the statutory right to compensatory interest in Yates' form division order is unenforceable because it contravenes a clear, strong public policy ... which mandates that interest owners be paid interest on funds that they are legally entitled to receive. Accordingly, we reverse the Court of Appeals, affirm the district court, and remand for further proceedings consistent with this opinion.' see *First Baptist Church v YATES PETROLEUM BT - P 3d* (2015) 345 310.

⁷⁸⁷ As in prima Paint

⁷⁸⁸ See *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d*; see also *First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 944 (1995). 'Applying the relevant state contract law, a court may . . . hold that an agreement to arbitrate is unenforceable based on a generally applicable contractual defense such as unconscionability.'

⁷⁸⁹ See i.e. *Parilla v. IAP Worldwide Services, VI, Inc.*, 368 F.3d 269, 275 (3d Cir. 2004), Courts should interpret arbitration clauses liberally.

⁷⁹⁰ See e.g. *Nagrampa v MailCoups, Inc BT - F 3d* (2006) 469 1257 [1269]'unlike Nagrampa's complaint, did not contain claims that the arbitration provision alone was void and unenforceable, but rather alleged that the arbitration provision was unenforceable because it was contained in an illegal usurious contract which was void ab initio. Id. at 1208. The opinion by the Florida Court of Appeal describes the claims of the plaintiff class in Buckeye: Appellees do not challenge the validity of the arbitration provision. Rather, they contend that the underlying contract is void ab initio because it is criminally usurious and, therefore, never existed at all. They further argue . . . that a trial court must determine the legal validity of the underlying contract before compelling arbitration.'

⁷⁹¹ *Nagrampa v. MailCoups, Inc. BT - F. 3d* 'While I believe that this contract is entirely valid under California law as construed by the courts in that state, the majority's exegesis of unconscionability doctrine does point to a disturbing trend of judicial hostility to form contracts.'

⁷⁹² *Nagrampa v. MailCoups, Inc. BT - F. 3d* 'unlike Nagrampa's complaint, did not contain claims that the arbitration provision alone was void and unenforceable, but rather alleged that the arbitration provision was unenforceable because it was contained in an illegal usurious contract which was void ab initio"...'While I believe that this contract is entirely valid under California law as construed by the courts in that state, the majority's exegesis of unconscionability doctrine does point to a disturbing trend of judicial hostility to form contracts.'

is contrary to the unconscionability doctrine,⁷⁹³ the situation is confusing and creates a conflict between Texas and California laws as well as others.⁷⁹⁴ California gives more consideration to the terms under the law,⁷⁹⁵ thereby enforcement of the award in such case is contrary to the public policy. California is more hostile to arbitration than Texas in this aspect.⁷⁹⁶ Although the parties are free to agree on any terms unless these terms are contrary to the applicable law to the contract and merit of dispute, the laws to be considered are the law applicable to the contract and the place of the enforcement in the stage of enforcing the arbitral award.

The separability principle facilitates the arbitration process by allowing the arbitrator to issue an award. Mistelis and Brekoulakis observe that the principle of separability is universally accepted, which should allow the arbitrator to issue an award on a contract whose legality is challenged.⁷⁹⁷ The Model Law expresses this principle clearly and provides that:

'an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. The decision by the arbitral tribunal that the contract is null and void shall not *entail ipso iure* the invalidity of the arbitration clause'.⁷⁹⁸

Likewise, to what is expressly provided in the Saudi Arbitration Law, where

'An arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. The nullification, revocation or termination of the contract which includes said arbitration clause shall not entail nullification of the arbitration clause therein, if such clause is valid.'⁷⁹⁹

⁷⁹³ See *Buckeye Check Cashing, Inc. v. Cardegna BT - US* In declining to apply Prima Paint's rule of severability, the Florida Supreme Court relied on the distinction between void and voidable contracts. 'Florida public policy and contract law,' it concluded, permit 'no severable, or salvageable, parts of a contract found illegal and void under Florida law.' Prima Paint makes this conclusion irrelevant. That case rejected application of state severability rules to the arbitration agreement without discussing whether the challenge at issue would have rendered the contract void or voidable. So also here, we cannot accept the Florida Supreme Court's conclusion that enforceability of the arbitration agreement should turn on 'Florida public policy and contract law'; In return see *Nagrampa v. MailCoups, Inc. BT - F. 3d* While I believe that this contract is entirely valid under California law as construed by the courts in that state, the majority's exegesis of unconscionability doctrine does point to a disturbing trend of judicial hostility to form contracts.'; See also *Williams v. CashCALL, INC.*

⁷⁹⁴ See *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* But because the forum selection clause requires Texas arbitration, the district court could not have simply severed it; the district court would have had to rewrite that paragraph in order to enforce it consistently with its (correct) unconscionability rulings. We find nothing to suggest that Plaintiffs will obtain an undeserved benefit from being able to avoid arbitration in this case; indeed, application of California law, and avoidance of the Texas arbitral forum, is consistent with the 'Addendum' the Plaintiffs received as part of the franchise agreement and were entitled to rely upon. Similarly, Fastbucks would not suffer any undeserved detriment by being forced to litigate this case in California court. Although Fastbucks's arbitration scheme is not illegal, it is inconsistent with California public policy concerning the rights of California franchisees... we AFFIRM the district court's holding that California law applies and renders the arbitration agreement unconscionable and accordingly, unenforceable. The case is REMANDED to the district court for further proceedings.'; See also *Williams v. CashCALL, INC.*

⁷⁹⁵ See *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* 'Having found the major part of the arbitration provision substantively unconscionable, is not illegal, it is inconsistent with California public policy..'

⁷⁹⁶ *Bridge Fund Capital Corp v Fastbucks Franchise BT - F 3d* (2010) 622 996 [1003].

⁷⁹⁷ Mistelis and Brekoulakis 54.

⁷⁹⁸ Art 16 (1) of the UNCITRAL Model Law. See 1040 (1) German Arbitration Act, that is based on Art 16 (1) of the UNCITRAL Model Law. Art 23.1 of the LCIA Rules further provide that "an arbitration clause which forms or was intended to form part of another agreement shall be treated as an arbitration agreement independent of that other agreement."

⁷⁹⁹ Art 21 of the Saudi Arbitration Law, likewise the Art 23 of the Egyptian Arbitration Law.

French law recognizes the separability principle and provides implicitly for the validity and enforceability of arbitration agreements.⁸⁰⁰ The English Arbitration Act also provides for the separability of arbitration agreements.⁸⁰¹ The arbitration agreement can still be binding even if the underlying contract never came into existence. However, under the principle of separability the arbitration agreement is valid unless it is directly challenged.⁸⁰² In the U.S., the arbitration clause in a contract exists independently from the rest of the contract.⁸⁰³ However, it is different whether the challenge is made to the arbitration clause or to the underlying contract or if the whole contract is affected by fraud as mentioned above. However, such jurisdiction with regards to who decides whether the validity of the contract or the validity of the arbitration agreement varies from one country to another.

5.4.1.2 The arbitration clause under an invalid contract according to *Sharia* law

Under Saudi law, an action to nullify an arbitral award shall not be admitted except if there is no arbitration agreement or if the agreement was void or voidable if the arbitrator have not applied the chosen law, or if the award was for matters not covered by the arbitration agreement.⁸⁰⁴ Thus, the question whether a contract that includes *Riba* would affect the validity of the arbitration agreement indirectly leads to non-arbitrability and intervention of courts either in Saudi Arabia or somewhere else. The contract containing interest may be considered invalid where the applicable law is *Sharia* law or where the award is enforced in a country that applies *Sharia*, such as Saudi Arabia.⁸⁰⁵ In *Sharia* law, there are several factors that determine whether a clause is valid or invalid. Generally, it is found invalid according to El-Ahdab in two categories, where first 'the clauses in question themselves are void, but the contracts remain valid,⁸⁰⁶ and second, 'the clauses are not only void in themselves but any contract containing them is also void'.⁸⁰⁷ Examples were given for the latter category of invalid clauses, such as clauses that contain *Riba* or fraud, called *Gharar*.⁸⁰⁸

Smolik observes according to the second category that 'the whole contract in which the agreement to arbitrate is embedded will also be found to be invalid'.⁸⁰⁹ El-Ahdab mentions that

⁸⁰⁰ Born, *International Arbitration: Cases and Materials* 61.

⁸⁰¹ S 7 of the Arbitration Act 1996; see also Born, *International Arbitration: Cases and Materials* 65.

⁸⁰² See *Fiona Trust & Holding Corporation and others v Privalov and others* [2010] EWHC 3199 (Comm)

⁸⁰³ *Mistelis and Brekoulakis* 70.

⁸⁰⁴ Art 50 of the Saudi Arbitration Law 2012.

⁸⁰⁵ See supra 496

⁸⁰⁶ El-Ahdab and El-Ahdab 22 ' These are clauses which, in fact, have no interest for the parties and their performance cannot be requested'.

⁸⁰⁷ *ibid*

⁸⁰⁸ El-Ahdab and El-Ahdab 21; Andrew Smolik, 'Effect of Shari'a on the Dispute Resolution Process Set Forth in the Washington Convention, The' [2010] J. Disp. Resol. 151, 166.

⁸⁰⁹ Smolik 166.

Sharia law does not prohibit arbitration clauses, but simply ignores them. *Sharia* law does not mention arbitration clauses and is silent about their validity, but the public policy mainly forbids clauses containing *Riba*.⁸¹⁰ According to El-Ahdab, 'even if the *Fiqh* does not mention arbitration clauses, they cannot be part of the category of invalid clauses associated with the contract ... [because] they do not contain interest (*Riba*) even if they constitute a contract within a contract, this second contract does not hide interest'.⁸¹¹ However, a contract that contains *Riba* would not lead to the invalidation of the whole contract but only to refusal to enforce the forbidden part (see Chapter Four). Even on the assumption that it invalidates the basic contract, invalidation of such contract does not affect the agreement to arbitration. *Sharia* gives general rules that can be applied to the contracts, whether to the underlying contract or to the agreement to arbitration (see Chapters Two and Four). There is no difference between any contracts in a general concept, where the arbitration agreement is subject to the freedom of the parties and the principle of *pacta sunt servanda* and good faith, and it is subject to the rules of the obligation (see Chapter Four). *Sharia* law distinguishes between the agreement to arbitration and the main contract, and therefore the invalidity of the main contract does not extend to such agreement, whether it is as a clause or separate.

Even if the enforcement of the award that contains *Riba* is contrary to *Sharia* and unenforceable, the rejection can be only under *Sharia* law applicable to the contract and dispute or under the place that applies *Sharia*. As a consequence, such action is accorded only in enforcement of the award that is contrary to *Sharia*, where the arbitration agreement is a reflection of the desire of the parties to submit to arbitration (see Chapter Four). Indeed, under *Sharia* law the contract containing *Riba* does not give effect to the invalidity of the agreement to arbitration, unless the arbitration agreement is itself invalid or does not exist. In general, *Sharia* law does not prohibit referral to arbitration despite the fact that these transactions are prohibited under *Sharia*. Nevertheless, the invalidity of the main contract does not affect the validity of the arbitral agreement, and including interest does not affect the ability to submit to arbitration. In principle, the agreement to arbitration is not contrary to *Sharia*, where it is merely a method to show the desire of the parties to submit to arbitration under such agreement.

According to Born there is a difference between the separability and competence-competence doctrines⁸¹² in the sense that the principle of separability may give more support for the jurisdiction of the arbitrators to decide the dispute if the arbitrator thinks that the invalid contract containing an arbitration clause. Such action may include a confirmation or rejection of the contract's terms of the parties which give effect to the validity of the contract, and therefore

⁸¹⁰ El-Ahdab and El-Ahdab 21.

⁸¹¹ El-Ahdab and El-Ahdab 23.

⁸¹² Born (n 22) 469.

whether or not such contract is void or voidable. Even if the parties select *Sharia* law as a law governing the contract, the arbitrators can use *Ijtihad* and *Qiyas*, where arbitrators have a power to decide such matters under *Sharia* law and consider each case separately. Thus, the validity of the arbitration agreement can be decided from the beginning.

The laws of many countries recognize the competence-competence doctrine equally to the Model Law, where 'the arbitral tribunal shall have the power to rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement',⁸¹³ which is similar to Art (20) of the Saudi Arbitration Law.⁸¹⁴ It is likewise in Egypt, where the law provides that the arbitrators shall decide over any jurisdiction-related claims including the existence, validity and scope of the arbitration agreement, where the parties explicitly agree.⁸¹⁵ Under the English law, the arbitrators have power to rule on its own jurisdiction,⁸¹⁶ where jurisdiction is broadly interpreted, and to adopt a robust "pro-arbitration" approach in the interpretation of international arbitration clauses.⁸¹⁷ The French law gives the arbitrator the authority to consider and decide all jurisdictional objections, whether directed to the underlying contract or to the arbitration agreement,⁸¹⁸ where it expressly grants arbitrators the power to decide challenges to their jurisdiction.⁸¹⁹

Recognition and enforcement of the arbitration agreement and of the arbitral award are separate processes.⁸²⁰ In international arbitration, the arbitrator must have the authority to decide the scope and the validity of the arbitration agreement as well as the authority to determine the outcome of the dispute under the applicable law, as a result of a natural consequence of the application of separability principle. However, 'because of the separability doctrine, certain claims regarding the underlying contract simply do not impeach or question the validity of the

⁸¹³ Art 23 (1) of the UNICTRAL Model Law, likewise Art 23 (1) of the LCIA Rules states 'the Arbitral Tribunal shall have the power to rule on its own jurisdiction, including any objection to the initial or continuing existence, validity or effectiveness of the Arbitration Agreement.'; AAA Commercial Arbitration Rule - R-7. Jurisdiction provides that: '(a) The arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope or validity of the arbitration agreement; (b) The arbitrator shall have the power to determine the existence or validity of a contract of which an arbitration clause forms a part. Such an arbitration clause shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitrator that the contract is null and void shall not for that reason alone render invalid the arbitration clause.'

⁸¹⁴ 'The arbitration tribunal shall decide on any pleas related to its jurisdiction, including those based on absence of an arbitration agreement, expiry or nullity of such agreement or non-inclusion of the dispute subject-matter in the agreement.'

⁸¹⁵ The Arbitration Act provides that the arbitral tribunal shall decide over any jurisdiction-related claims including the existence, validity and scope of the arbitration agreement.

⁸¹⁶ The Arbitration Act, 1996, s 23, and 30 "Unless otherwise agreed by the parties, the arbitral tribunal may rule on its own substantive jurisdiction, that is, as to – (a) whether there is a valid arbitration agreement, (b) whether the tribunal is properly constituted, and (c) what matters have been submitted to arbitration in accordance with the arbitration agreement.";

⁸¹⁷ Born, *International Arbitration: Cases and Materials* 65.

⁸¹⁸ Born (n 22) 469.

⁸¹⁹ Born, *International Arbitration: Cases and Materials* 61.

⁸²⁰ Mann and Roberts 64; Villiers; Berg, 'New York Convention of 1958: Refusals of Enforcement.'

arbitration agreement, and therefore must be resolved by the arbitrators'.⁸²¹ Arbitrators generally possess broad power,⁸²² and the arbitrator should make sure that the award and the arbitration agreement would be enforced according to the applicable law, provided the arbitration agreement is valid according to Art II of the NYC.

5.4.2 *The scope of arbitration*

Even when the validity of an arbitration agreement is confirmed, issues may arise during the course of the arbitration if one of the parties alleges that the arbitral tribunal is exceeding the scope of its authority.⁸²³ Art V (1) (c) of the NYC gives exception for non-enforcement of a foreign award on two grounds, either if the determination of the award was not based on the terms of submission to arbitration or else if it contains matters beyond the scope of such submission.⁸²⁴ This article applies where a valid arbitration agreement exists but the arbitral tribunal has exceeded its authority.⁸²⁵ Such exception would not be only at the request of one party under the court of the enforcement place under Art V (1). Kurkela and Turunen observe

this Art belongs to the group of “weak” grounds requiring party action and proof in order to non-enforcement, which ‘can be divided into two subsections...the award deals with a difference beyond the scope of the submission to arbitration (i.e., the arbitration agreement or clause; or ... the award contains decisions on matters beyond the scope of the submission to arbitration.’⁸²⁶

The content and scope of arbitrability is a matter of parties’ agreement or domestic law of each separate state which applies conflict of laws given the internationality of arbitration. However, when this conflict persists, issues remain as to who is responsible to determine the rate and period of interest, whether this is explicitly provided in the contract or not, and whether the rate of interest or the period falls outside the scope of the authority of the arbitrator.

⁸²¹ Bom (n 22) 470.

⁸²² Bom 2619.

⁸²³ United Nations, ‘The Arbitration Agreement’ (2005) 7 <http://unctad.org/en/Does/cdmmisc232add39_en.pdf>.

⁸²⁴ ‘The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced’; see also Art 34 (2) (a) (iii) of the Model Law. According to many arbitration laws such as Act 53 of the Egyptian law, and as in Art 50 (f) and (g) of the Saudi Arbitration Law, s 13 (3) of the Arbitration Act 1996 ‘In determining for the purposes of the Limitation Acts when a cause of action accrued, any provision that an award is a condition precedent to the bringing of legal proceedings in respect of a matter to which an arbitration agreement applies shall be disregarded’, as a mandatory rule.

⁸²⁵ Kronke 258.

⁸²⁶ Matti Kurkela and Santtu Turunen, *Due Process in International Commercial Arbitration* (Oxford University Press 2010) 29.

In the U.S., courts resolve doubts about arbitrability in favour of arbitration.⁸²⁷ In addition, the parties must agree to arbitrability⁸²⁸ and determine the dispute and interest rate.⁸²⁹ In *Tricon Energy Ltd. v. Vinmar Intern. Ltd.*, the court held that parties did not refer to post-judgment interest.⁸³⁰ The court intervened and determined the post-judgment rate,⁸³¹ or compensation.⁸³² Some courts will refer the determination regarding the scope of the arbitration agreement to the arbitrators, whether the arbitration agreement is determined broadly.⁸³³ In contrast, even if the

⁸²⁷ *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983); *United Steelworkers of Am. v. Warrior & Gulf Navigation Co.*, 363 U.S. 574 (1960); *Parsons & Wh. Ov. Co., Inc. v. SOCIETE G. DE L. DU P.(R.)*, 508 F.2d 969 (2d Cir. 1974); see also *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989).

⁸²⁸ *First Options of Chicago, Inc. v. Kaplan, the U.S.*, 514 U.S. (U.S. S. Ct. 1995) at [939] held that one party 'did not agree to arbitrate arbitrability', 'courts should not assume that the parties agreed to arbitrate arbitrability unless there is "clear and unmistakable" evidence that they did so'; *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. U.*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989) at 485 'Arbitration is, of course, "a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit.'" 'Not only does the FAA require the enforcement of arbitration agreements, but we have held that it also establishes substantive federal law that must be consulted in determining whether (or to what extent) a given contract provides for arbitration'. id 486

⁸²⁹ *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013) at [453] '[A]rbitration is simply a matter of contract ...; it is a way to resolve those disputes — but only those disputes — that the parties have agreed to submit to arbitration.' *First Options*, 514 U.S., 115 S. Ct. 1920 at [943]. Unless the parties agreed to submit the question of arbitrability to arbitration, the court must decide the question independently, "apply[ing] ordinary state-law principles that govern the formation of contracts.' *Tricon Energy Ltd.* at [457] "That principle does not decide this case; if the arbitrators awarded a nonstatutory rate, they did so based on the parties' submission of the issue to them, not on their own authority. An arbitration panel "may determine whether the parties have sufficiently contracted for their own rate and, if they have, indicate that rate should be applied."; see *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013) at [458] "Because the parties agreed to submit the issue of postjudgment interest to arbitration, the arbitration panel had the authority to award a non-statutory rate."; id 460 'If an arbitration panel has been granted authority by the parties to award a nonstatutory rate of postjudgment interest, and if it wishes to do so, it must expressly award "postjudgment interest." This panel did not.'; see *Newmont USA v. Insurance Co. of North America*, 615 F.3d 1268 (10th Cir. 2010) at [1275] 'Our cases hold unless the parties to an agreement "clearly and unmistakably" provide otherwise, "the question of arbitrability—whether a contract creates a duty for the parties to arbitrate the particular grievance—is undeniably an issue for judicial determination.'; id at [1277] 'An agreement to apply a post-judgment interest rate other than that § 1961 specifies is enforceable so long as the parties indicate their intent to override the statute using "clear, unambiguous and unequivocal language." ... Consistent with § 1961, an arbitration panel may not establish a post-judgment interest rate itself, but it may determine whether the parties have sufficiently contracted for their own rate and, if they have, indicate that rate should be applied.' See *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013); see also *NEWMONT USA v. Insurance Co. of North America*, 615 F.3d 1268 (10th Cir. 2010), if the arbitrators awarded a non-statutory rate, they did so based on the parties' submission of the issue to them, not on their own authority. An arbitration panel "may determine whether the parties have sufficiently contracted for their own rate and, if they have, indicate that rate should be applied." Id. Furthermore, the parties may agree to submit the question of post-judgment interest to arbitration.

⁸³⁰ *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013) at [459].

⁸³¹ *Tricon Energy Ltd.* at [451] 'Tricon cross-appeals, contending the district court improperly granted post-judgment interest at the statutory rate instead of the rate assigned by the arbitrators.' ... Id 456 'Tricon appeals the award of postjudgment interest at the federal statutory rate, contending that the court impermissibly disregarded the arbitrator's award of a higher rate'; id 456 'governs a district court judgment confirming an arbitral award even when the arbitrators awarded postjudgment interest at a different rate.'... The one circuit that has confronted the question held that the district court had erred by replacing the awarded rate with the statutory default'; see *Newmont USA v. Insurance Co. of North America*, 615 F.3d 1268 (10th Cir. 2010) at [1272] 'the district court erred by altering the arbitration panel's post-judgment interest rate determination and setting the post-judgment interest accrual date, the district court should have applied the post-judgment interest rate set forth in the parties' agreements and incorrectly determined the start date for the accrual of post-judgment interest.'

⁸³² *Parsons & Wh. Ov. Co., Inc. v. SOCIETE G. DE L. DU P.(R.)*, 508 F.2d 969 (2d Cir. 1974) at [978]

⁸³³ See, e.g., *Sedco*, 767 F.2d at 1145; see also 31 Am. JUR. 3d Proof of Facts 495, § 9.

parties agree on interest, the court may intervene in case the arbitrator does not determine whether the interest is simple or compound,⁸³⁴ or pre- or post-award.⁸³⁵ However,

“[T]he U.S. has no federal statute governing awards of prejudgment interest on international arbitral awards”; as a result, whether and at what rate to apply post-award, prejudgment interest where it is not specified in the arbitral award itself is left to the discretion of the court’.⁸³⁶

The governing federal law does not give the district courts the power to alter or reform the terms of the arbitral award that were set by the arbitrator.⁸³⁷ Under federal law, ‘arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit’.⁸³⁸ However, ‘any doubts concerning the scope of arbitrable issues should be resolved in favour of arbitration’.⁸³⁹ In addition, a broad arbitration clause gives rise to the presumption of arbitrability.⁸⁴⁰ Thus, if it is determined that an arbitration agreement exists and the dispute falls within the scope of the agreement, the FAA requires the court to refer the matter to arbitration proceedings.⁸⁴¹

⁸³⁴ *Avr Communications, Ltd. V. American Hearing Systems, INC.*, Civil No. 13-3027 (JNE/TNL) (D. Minn. Jan. 31, 2014) ‘the parties disagree about whether the interest specified in the Court’s Order of January 31, 2014 should be simple or compound. As this is an action to confirm a foreign arbitral award, the language of the Order reflects the language of the arbitrator’s award. The arbitrator specified that interest is to be charged at a rate of 4% per annum, but was silent as to whether it is to be calculated with a simple or compound formula.’

⁸³⁵ *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013) at [457] Furthermore, the circuits have unanimously agreed that “an arbitration panel may not establish a post-judgment interest rate itself...”; *Tricon Energy Ltd. v. Vinmar Intern., Ltd.*, 718 F.3d 448 (5th Cir. 2013) at [458] “Nothing in the cases cited by Vinmar counsels a different approach. In *Durga Ma*, 387 F.3d at 1022, for example, the arbitration panel stated, “The total amount of this award ... shall bear interest at the statutory rate from [the date of the award].” The panel did not specify a state rate rather than the federal rate and did not distinguish postjudgment from prejudgment interest. ... there is no indication that the parties in *Durga Ma* submitted the issue of postjudgment interest to arbitration or that the arbitration panel was purportedly interpreting the contract.”; *id* 460 ‘Although Tricon asked for postjudgment interest expressly, the panel did not award postjudgment interest expressly. Under the award’s residual clause — “All claims not expressly granted are hereby denied” — the arbitrators denied Tricon’s request.’; *Tricon Energy Ltd.* at [456] ‘the arbitrators in this case did not award postjudgment interest, but post-award interest, and that distinction makes a difference.’

⁸³⁶ *Avr Communications, Ltd. V. American Hearing Systems, INC.*, Civil No. 13-3027 (JNE/TNL) (D. Minn. Jan. 31, 2014)

⁸³⁷ *Avr Communications, Ltd. V. American Hearing Systems, INC.*, Civil No. 13-3027 (JNE/TNL) (D. Minn. Jan. 31, 2014). As a result of the court’s error ‘the arbitration panel had the authority to decide the post-judgment interest issue. See *Newmont USA v. Insurance Co. of North America*, 615 F.3d 1268 (10th Cir. 2010) at [1276].

⁸³⁸ *Republic of Ecuador v Chevron Corp BT* at [392].

⁸³⁹ *Newmont USA v. Insurance Co. of North America*, 615 F.3d 1268 (10th Cir. 2010) at [1275]. As a result, we resolve “any doubts concerning the scope of arbitrable issues . . . in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability”. See *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 103 S. Ct. 927, 74 L. Ed. 2d 765 (1983) at 24-25; see also *Republic of Ecuador v. Chevron Corp.*, 638 F.3d 384 (2d Cir. 2011) [392-393]

⁸⁴⁰ *Id* [1276]

⁸⁴¹ *Margaret O’Shea. v. Direct Financial Solutions, LLC, d/b/a Cash Central, Civil Action* [3]; see also *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 632 (1985) ‘Just as it is the congressional policy manifested in the Federal Arbitration Act that requires courts liberally to construe the scope of arbitration agreements covered by that Act, it is the congressional intention expressed in some other statute on which the courts must rely to identify any category of claims as to which agreements to arbitrate will be held unenforceable. By agreeing to arbitrate a statutory claim, a party does not give-up the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.’

In Egypt for example, the law requires that the subject matter of the dispute must be determined.⁸⁴² However, the arbitral award may be refused due to the scope of the arbitration or the authority of the arbitrator⁸⁴³ if the award excluded the application of the law chosen by the parties to govern the merits or if the proceedings were void where they affect the award itself. Parties may claim compensation in absence of express reference to the specific dispute and if the arbitration agreement is not limited to purely contractual claims.⁸⁴⁴ However, non-arbitrability is not explicitly mentioned as a ground for set-aside, but it is considered practically a variation of public policy (see Chapters Four and Six) which allows for the refusal of arbitral awards. Some countries may intervene in the jurisdiction of the arbitrator, thereby the objection can be made if the arbitrator is exceeding its substantive jurisdiction⁸⁴⁵ or if the appeal can be made that the award exceeded the scope of the arbitration, although the arbitrator has a jurisdiction to decide such scope.⁸⁴⁶ In France, when the award is challenged, the court will refuse to enforce the award if it leads to breach of international public policy.⁸⁴⁷

The arbitration agreement provides the basis for arbitration. It is defined as an agreement to submit present or future disputes to arbitration. This generic concept comprises two basic types: a) A clause in a contract, by which the parties to a contract undertake to submit to arbitration the disputes that may arise in relation to that contract (arbitration clause); or b) An agreement by which the parties to a dispute that has already arisen submit the dispute to arbitration (submission agreement). The arbitration clause therefore refers to disputes not existing when the agreement is executed. Such disputes, it must be noted, might never arise. That is why the parties may define the subject matter of the arbitration by reference to the relationship out of which it derives. The submission agreement refers to conflicts that have already arisen. Hence, it can include an accurate description of the subject matters to be arbitrated.⁸⁴⁸

⁸⁴² Art 10 of the Egyptian Arbitration Law 'The arbitration agreement may be concluded before the dispute has arisen either in the form of a separate agreement or as a clause in a given contract concerning all or certain disputes which may arise between the two parties. In the latter case, the subject matter of the dispute must be determined in the Request for Arbitration referred to in paragraph 1 of Article 30 hereof. The arbitration agreement may also be concluded after the dispute has arisen, even if an action has already been brought before a judicial court, and in such case, the agreement must indicate the issues subject to arbitration, on penalty of nullity.'

⁸⁴³ *Hotel Company v Construction Company, Final Award, CRCICA Case No 730/2011, 18 February 2013*, Arbitral Awards of the Cairo Regional Centre for International Commercial Arbitration IV, (Kluwer Law International 2014) 371 – 396; see *Contractor (Egypt) v. Employer (Egypt), Final Award, CRCICA Case No. 730 of 2011* reported in Albert Jan van den Berg (ed), *Yearbook Commercial Arbitration 2013 - Volume XXXVIII*, Yearbook Commercial Arbitration, Volume 38 (Kluwer Law International 2013) 32 – 50; see also Jalal El-Ahdab (ed), 'African Company for Environmental Services (the "Company") v General Association for Cleaning (the "Association")', Final Award, CRCICA Case No. 394/2004, 28 September 2005' (2009) 1 *International Journal of Arab Arbitration* 383. "The tribunal is not competent to examine the requests of the Claimant Company related to the deductions of social insurance, tax on sales, and tax on industrial and commercial profits... the Respondent shall pay to the Claimant Company an amount of ... Million USD with an annual interest of 7%. ...The tribunal rejects the remainder of the Claimant's claims".

⁸⁴⁴ *Ibid.*, Para 22 "the scope of the arbitration clause is not [limited] exclusively to purely contractual claims, but also encompasses tortious claims, if any."

⁸⁴⁵ See s 31 of the Arbitration Act, 1996. But only in case unfair terms and indirect good faith see Chapter Four.

⁸⁴⁶ Art 50 of the Saudi Arbitration Law, but 'if parts of the award relating to matters subject to arbitration can be separated from those not subject thereto, then nullification shall apply only to parts not subject to arbitration'.

⁸⁴⁷ See e.g Bars and Kaminsky.

⁸⁴⁸ United Nations. 'The Arbitration Agreement' 3.

The arbitration agreement should be treated as a distinct agreement⁸⁴⁹ and any matters related to commercial disputes are arbitrable under a valid arbitration agreement. It is rare for an arbitration clause to provide for the arbitration of any disputes that may arise between the parties, but typically they provide for arbitration of disputes arising from a particular relationship, usually the substantive contract in which it is embedded.⁸⁵⁰ If there is no such reference, disputes may still be covered by the arbitration clause contained in the original agreement.⁸⁵¹ It was thought that an arbitration agreement would not apply to the arbitration of ex-contractual claims, but they fall within such agreement where there is a sufficient link to the contractual relationship established between parties.⁸⁵²

A valid agreement to arbitrate may contain some general terms such as the choice of law or place of arbitration etc. or merely refer to arbitration. The arbitration agreement may also include specific terms such as the determination of interest rate and time period, whether in the contract itself or in the arbitration agreement. The parties cannot rely on the scope of the arbitration as a ground for refusal in all cases when a link between the disputes and contract can be made and where there is an arbitration agreement manifesting the parties' wishes to subject their disputes to arbitration.⁸⁵³

The scope of arbitration is determined under laws governing the arbitration agreement which provides arbitrators the authority and the power, whether general or specific, and whether express or implicit. The arbitrator according to his authority and jurisdiction⁸⁵⁴ is allowed to determine the interest rate and period. However, uncertainties regarding the scope of the arbitration clause often lead to disputes concerning the jurisdiction of the arbitrator.⁸⁵⁵ The determination of the scope of arbitration clauses remains difficult, in particular if the intent of the parties cannot be established.⁸⁵⁶ Nonetheless, once the arbitrator establishes his own jurisdiction, the scope of submission shall be determined by him at the first instance, and possibly reviewed by enforcing court.⁸⁵⁷

⁸⁴⁹ As the legal action of "s 7 of the Arbitration Act 1996".

⁸⁵⁰ Michael Pryles and Jeffrey Waincymer, 'Multiple Claims in Arbitrations Between the Same Parties' 3.

⁸⁵¹ Irene Welser and Susanne Molitoris, 'The Scope of Arbitration Clauses—Or "All Disputes Arising out of or in Connection with This Contract..."' [2012] Austrian Yearbook on International Arbitration 17730, 30.

⁸⁵² Pryles and Waincymer 3.

⁸⁵³ See e.g. Award in ICC Case No.6474 of 1992, XXV Y.B. Comm. Arb. (2000) 279, 283 'In international commercial arbitration, the first and foremost duty of the arbitrator is undoubtedly to base his decisions, whether relating to jurisdiction or to the merits of the dispute, on the common will of the Parties, regarding for instance the applicable law.'

⁸⁵⁴ I.e. see Art 20 of the Saudi Arbitration Law, see s 30 of the Arbitration Act 1996, see Art 21 (5) of the Swiss Rules of International Arbitration 'The arbitral tribunal shall have jurisdiction to hear a set-off defence where the relationship out of which this defence is said to arise is not within the scope of the arbitration clause or is the object of another arbitration agreement or forum selection clause.'

⁸⁵⁵ Welser and Molitoris 17.

⁸⁵⁶ Welser and Molitoris 30.

⁸⁵⁷ Pryles and Waincymer 47.

5.4.3 *The applicable law to the contract and the dispute*

The arbitrator works within three potential constraints—the applicable law, the parties' agreement and the national courts. With regards to the interest rate and time period, the scope of the dispute will be determined by either the terms of the contract or the terms of arbitration agreement itself under the applicable law according to the authority and the power of the arbitrator. However, the scope of the authority and jurisdiction of the arbitrator would be determined under the law applicable to the arbitration agreement.⁸⁵⁸ Interest can be governed by either the terms of the parties in the contract or the law applicable to the merits of dispute. It is possible that the parties determine the law governing the contract and disputes, in addition they may choose their contract terms or may fail in one or both choices.

Giardina emphasizes that arbitrators can freely determine interest without any reference to the law governing the contract in cases where the arbitration rules applicable to the procedure allow them to do so.⁸⁵⁹ It is argued that the terms of the contract should take priority over the applicable law, or that the chosen law will apply only in absence of such terms, if they are excluded from the law chosen and therefore will not be governed by any law.⁸⁶⁰ In addition, in the event that the place of enforcement is England, 'the power to award statutory interest may be excluded by a contractual provision which provides for interest at a different rate or for no award of interest',⁸⁶¹ '[t]he parties, it has to be assumed, have deliberately agreed to give jurisdiction to an arbitrator to decide on the rate of interest, including interest for the period between the award and payment of the amount awarded'.⁸⁶² It has been argued that 'what counts at exequatur stage is only the legal result of the arbitral decision and not the rules of law employed to reach it'.⁸⁶³ However, the law applicable to the contract determines the limitation of the parties' freedom and

⁸⁵⁸ See chapter three and as a legal action In *Arsanovia Ltd & Ors v Cruz City 1 Mauritius Holdings* [2012] EWHC 3702 (Comm), the arbitration agreement was governed by LCIA Arbitration and the law governing the dispute was Indian law. *Id* at [3–4] The claimants argued that the arbitral tribunal has no jurisdiction where the law applicable to arbitration agreement was Indian law that determines the scope of the arbitration. *Id* at [6] Under the closest and most real connection test under some discussion the court find that the English law applied to arbitration agreement, therefore the arbitral tribunal has jurisdiction.

⁸⁵⁹ Giardina 140, he refers also to Article 60 of the WIPO Rules, which regulates currency and interest with respect to the sums to be awarded, provides that

'the Tribunal may award simple or compound interest to be paid by a party on any sum awarded against that party. It shall be free to determine the interest at such rates as it considers to be appropriate, without being bound by legal rates of interest, and shall be free to determine the period for which the interest shall be paid.'

⁸⁶⁰ UNITED NATIONS, 'UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT; The Law Governing the Merits of the Dispute' 11; see also United Nations, 'The Arbitration Agreement' 54 'At any rate, irrespective of the substantive law that the parties or the arbitrators, as the case may be may have determined as applicable in all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction (article 28.4, Model Law).'

⁸⁶¹ *Yukos Capital SARL v OJSC Rosneft Oil Co* [2014] EWHC 2188 (Comm) (Lord Gribner) [75].

⁸⁶² *Ibid* (Megaw LJ) [76].

⁸⁶³ Fabrizio Marrella, 'Choice of Law in Third-Millennium Arbitrations: The Relevance of the UNIDROIT Principles of International Commercial Contracts' (2003) 36 *Vand. J. Transnat'l L.* 1137, 36.

the power of the arbitrator. This is similar to effects of the law applicable to the arbitration agreement in determining the jurisdiction of the arbitrator with regards to the scope of the dispute.

If the arbitrator ignores the applicable law, the award may be set aside,⁸⁶⁴ thus the award will not become binding to the parties. Art V (1) (e) does not provide whether the award would be set aside under the law applicable to the arbitration agreement or the law applicable to the dispute (see Chapter Three). It may be set aside under the substantive law applicable to the contract and dispute. In *Yukos Capital SARL v OJSC Rosneft Oil Company*,⁸⁶⁵ the awards⁸⁶⁶ was set aside by a Russian court,⁸⁶⁷ where the governing law is Russian law. The Russian courts had set the awards aside,⁸⁶⁸ therefore, there is no basis for awarding interest.⁸⁶⁹ However,

[I]n England it is suggested that where [an award] has been set aside in the court of the seat, an arbitral award should be enforced only if recognition of the order setting aside the award would be impeachable for fraud or as being contrary to natural justice, or otherwise contrary to public policy.⁸⁷⁰

In Egypt, an arbitral award may not be annulled solely on the basis of a mistake or error in the application of the applicable Egyptian law only in case of total exclusion of the law chosen by the parties to govern the merits of the dispute.⁸⁷¹ In Saudi Arabia, the award may be set aside when such law is contrary to *Sharia*. However, such action shall not be applied based only on the fact that *Sharia* law is the applicable law. To further clarify, the award cannot be set aside unless the arbitrator clearly ignores the express law to the dispute or the implicit law applicable according to the closest connection test.

⁸⁶⁴ According to Art V (1) (e) 'The award has not yet become binding on the parties, or has been set aside or suspended by competent authority, of the country in which, or under the law of which, that award was made.'

⁸⁶⁵ *Simon J in Yukos Capital SARL v OJSC Rosneft Oil Co [2014] EWHC 2188 (Comm)*.

⁸⁶⁶ The awards did not contain provision for the payment of interest, and no interest was paid in respect of late payment the principal sums which had been awarded. *id* at [5], 'These claims have been advanced under Article 395 of the Russian Civil Code and/or s.35A of the Senior Courts Act 1981.'

⁸⁶⁷ *Ibid* 'The Defendant has pleaded (among other points) that, as a consequence of the Russian Set-aside Decisions, (a) the Awards no longer exist in a legal sense (under the principle *ex nihilo nil fit*, or, 'nothing comes of nothing'), and (b) that the Claimant is precluded from asserting that the Awards are valid and binding on the parties. It has also advanced a number of other reasons why post-award interest is not recoverable. The Claimant denies the defences based on the *ex nihilo nil fit* principle and issue estoppel.' ... 'The issue is whether the Set-aside Decisions have the effect that the Awards cannot be enforced at Common Law because they no longer exist in a legal sense.' at [9]

⁸⁶⁸ In the set-aside Decisions, they no longer exist as a matter of Russian law. *Id* at [10].

⁸⁶⁹ *Ibid* at [10]

⁸⁷⁰ *ibid* at [12] In addition, there were no Russian exequaturs in respect of the awards; interest is not recoverable on the principal sum as a matter of Russian law. *Id* at [64-68] 'It was common ground between the experts that since 26 May 2011 (the date of the Resolution 10-P decision) no Russian Court had treated that decision as having changed the law in relation to post-award interest.' However, there is no absolute bar to the award of interest in respect of the late payment of a foreign award under s.35A of the Senior Courts Act 1981. *Id* at [79] Thus, post-awards cannot be recovered as a matter of Russian law and interest on the sums claimed in the English proceedings can be recovered under s.35A of the Senior Courts Act 1981. *Id* at [81] In England, 'there is no principle of *ex nihilo nil fit*...to prevent the English court giving effect to the Awards' *id* at [81]

⁸⁷¹ Art 53 (1) (d) of the Egyptian Arbitration Law. Any erroneous application of the applicable law should not result to set-aside except in cases where the error is of such gravity that it amounts to a total exclusion of the applicable law. See National Cement Company (the respondent) requested the annulment of International Chamber of Commerce (ICC) arbitral award CK/9928 rendered on December 21 1999 in arbitral proceedings commenced by Andritz Company (the plaintiff) and others.

Article V (1)(e) of the NYC provides for annulment or non-recognition of the arbitral award if it is set aside or suspended by the country of the chosen law or the law of the seat of arbitration in the absence of choice.⁸⁷² This reflects the authority of arbitrators to consider substantive law under applicable law in the event that one of them is applicable to the dispute in the absence of the other. It gives courts the right to review such arbitral awards at the request of the parties. There are varying views about the retention of such articles and their affects on the authority of the arbitrator⁸⁷³, although the theory takes into account that the parties choose the applicable law in all cases. Neither the competent court nor the country of enforcement should intervene in the arbitral award without a request of one of the parties. The obligation of contracting states to recognize awards without engaging in any substantive review of the merits of the award applies without regard to the arbitrators' choice of law decisions concerning the applicable substantive law.⁸⁷⁴

Sometimes the parties have chosen a law they want the dispute to be subject to, others may leave such choice to the arbitrator as a general authority to determine such an issue (see Chapter Three). The arbitrator with jurisdiction can determine the applicable law, taking into account whether the agreement to arbitration is separated or connected to the underlying contract and whether the parties' choice of law(s) is express or implicit. There are some factors that would give effect to the determination of the substantive law applicable to the dispute (see Chapter three).

Some jurisdictions have clear control over the law applicable to the contract, whether express or implicit, and whether under the arbitration seat or under the law applicable to the arbitration agreement.⁸⁷⁵ In addition, in such jurisdictions conflicts may arise between the law of the seat of arbitration and the law that has been chosen by the parties. Some are limited to

⁸⁷² 'The award has not yet become binding on the parties, or has been set aside or suspended by competent authority of the country in which, or under the law of which, that award was made.'; Article 34 (2)(a) I and 26 (1)(a) I of the model law that the arbitrable award can be set aside or rejected the recognition if it is validity according to the law that has been chosen by the parties or according to the arbitration seat in event failing so do.

⁸⁷³ Albert Jan van den Berg, 'ARTICLE Should the Setting Aside of the Arbitral Award Be Abolished?' [2014] ICSID Review 1 'The length of this lecture already demonstrates that the current status of setting aside in international arbitration requires a lot of explaining. This is due in part to the limited scope and outdated provisions of the New York Convention and the copying of the New York Convention into the UNCITRAL Model Law.'; Born (n 22) 2625 'neither the New York Convention nor national arbitration legislation make any provision for annulment or non-recognition of awards based on the arbitrators' application of the "wrong" substantive law or conflict of laws rules.'

⁸⁷⁴ Born (n 22) 2620.

⁸⁷⁵ In United States, the courts intervene in all cases in the law governing the contract, whether the law of the arbitration seat applies or the law of the parties' place. Saudi law interferes in the choice of the applicable law; therefore it leads to a narrowing of the freedom of the parties and the application of Sharia law indirectly. The arbitral tribunal in the Egyptian Arbitration seat, may take into account the Egyptian law with regard to interest rates and periods, however, this measure could result in other legal implications with respect to enforcement. See *EU Joint Venture of Three Companies (Contractor) v. An African Tourism Company (Owner)*, Final Award, CRCICA Case No. 175/2000, 28 December 2008, Arbitral Awards of the Cairo Regional Centre for International Commercial Arbitration IV, (Kluwer Law International 2014) pp. 73 – 183, see also *Malicorp Ltd. (UK) v. The Government of the Arab Republic of Egypt and others*, Final Award, CRCICA Case No. 382/2004, 7 March 2006

whatever is allowed under the substantive law of the contract, by mandatory laws in effect at the arbitration seat.⁸⁷⁶ However, the law applicable to the arbitration agreement is not necessarily the same substantive law applicable to the underlying agreement or relationship.⁸⁷⁷ Dicey and Morris emphasize the proper law of the contract under which a debt is incurred determines the interest rate.⁸⁷⁸ However, such law can govern the contract and dispute unless the parties' choice the law expresses otherwise. Regardless of the impacts of the arbitration seat or the law applicable to the arbitration agreement, the applicable law to the contract and dispute shall governs the terms of the contract, expressly or implicitly.

The arbitrator should consider the parties' clauses on the contract unless such terms violate the substantive law applicable to the contract (see Chapter Four). Thus, if the parties fail to specify interest rate and period, the contract will be governed by the applicable law. Many national arbitration laws gives the arbitrator the right to issue the award as it deems appropriate if the parties fail to do so (see Chapter Three).⁸⁷⁹ In some jurisdictions, the law applicable to the arbitration agreement determines the jurisdiction of the arbitrator. This law may or may not be the same as the law governing the contract. If the parties fail to specify the choice of laws, the arbitrator shall award interest according to the parties' agreement subject to mandatory rules on *Riba*. In the absence of the agreement, the arbitrator has a power to award the interest according to general practice.⁸⁸⁰

5.4.3.1 *Ijtihad* principle under Sharia law

The principle of *Ijtihad* is to provide an interpretive understanding of the Islamic texts so as to come up with a contextual approach to each issue through interpretation of the measures that were in place in the *Quranic* revelation era, and to compare them to modern interpretations of arbitration (see Chapter Two). Arbitrators must not have undue restrictions on interpreting the law but rather restrictions that reflect moral and ethical limitations. The principle of *Ijtihad* can

⁸⁷⁶ In France, the parties' choice of law will only to mandatory laws if enforcement of the award would breach the international public policy of the seat. English law gives effect to mandatory rules in the event of explicit choice, or to conflict of laws rules in the seat in the event of default of choice; this results in any case to the application of the Arbitration Act, 1996 regardless of other considerations. Section 49 of that Act gives the absolute freedom of the arbitrators to award interest, regardless of all other considerations.

⁸⁷⁷ Kurkela and Turunen 30.

⁸⁷⁸ Dicey and Morris, *The Conflict of Laws* (Lawrence Collins ed, 11th edn, Sweet & Maxwell Ltd 1987) 1331; see also Hunter and others 13 'As to pre-award interest, where there is an agreement between the parties that provides for "contractual interest", both the question of the liability to pay interest and the amount to be paid (including the period and the rate) are to be determined by the proper law of the contract under which the debt is incurred'.

⁸⁷⁹ As a legal action of Art 28 (4) of AAA 'the tribunal may award such pre-award and post-award interest, simple or compound, as it considers appropriate, taking into consideration the contract and applicable law.' Also as a legal action of s 49 of the Arbitration Act 1996.

⁸⁸⁰ See *Bosack v. Soward*, F.3d (WL 3416227, 9th Cir., 2009) 'Federal courts have uniformly held that absent some requirement in the agreement, "[a]rbitrators are not required to set forth their reasoning supporting an award.'

be used to define arbitrability, particularly in cases that involve contracts that contain forbidden elements under Islamic law, such as *Riba* and issues of substantive law that may invalidate them.

The issues surrounding arbitration proceedings are, like all other Islamic issues, centred on an interpretation of the *Quran* and of the secondary sources. A central concept to *Ijtihad* and *Qiyas* in its analytical and interpretative function is to interpret the law within the appropriate context. The arbitrator can use this context to issue awards and choose some of the views of other Islamic schools as long as they keep within the principles of *Sharia*. This very idea demands almost a reinterpretation of the concepts of Islam today dating back to the early days of Islam.

If the award was issued in accordance with the principles of *Ijtihad* and *Qiyas* and based on the main sources of *Sharia*, it is logical that there would be no need to reject the award. The concerns of *Sharia* lie in the applicable law and the power of the arbitrator, which may lead to the enforcement of a foreign law. These concerns may be summarized in the enforcement of foreign arbitral awards. In case *Sharia* law is the law applicable to dispute, it cannot be set aside even if the contract or the terms of the parties deemed invalid, unless they are contrary to the main sources of *Sharia* law, when it is possible to apply the *Ijtihad* theory.

Arbitration proceedings and awarding interest depends on the arbitrator's authority. In fact, that the doctrine of *Riba* does not prohibit the awarding of interest,⁸⁸¹ as not every interest is *Riba* (see Chapter Four). Thus, *Riba*, which exceeds the allowable interest rate on interest-based loan contracts, is contrary to *Sharia* law. By using the *Ijtihad* principle on awarding interest with respect to compensation or loan contracts, a distinction can be made between the two. To prevent the refusal of awards, it is advisable to consider each dispute on a case-by-case basis by considering the rules of *Sharia*, the freedom of the parties,⁸⁸² and whether the contract expressly contains *Riba*.

5.5 The non-arbitrable under the enforcing court

The New York Convention Art V (2) (a) also set forth a provision with regards to non-arbitrable or substantial arbitrability, which states that recognition and enforcement of an arbitral award may be refused if the court where such recognition and enforcement is sought finds 'the subject matter of the difference is not capable of settlement by arbitration'. It may apply to the subject matter of the dispute, although it was considered arbitrable with a valid arbitration agreement under the law of the country where the award is made, or under the applicable law. However, the action in Art V (2) (a) is considered under the law of the country where recognition

⁸⁸¹ Where "the doctrine of *riba* did not prohibit the awarding of interest" in *Contractor v Employer*, Final Award, ICC Case No. 7063, 1993 in Berg, 'Yearbook Commercial Arbitration' 87-91.

⁸⁸² In event the dispute is according to the Shari'a law or the enforcement of the award is in e.g. Saudi Arabia.

and enforcement of the award is sought. This provision has a similar effect as those of Art II (1) of the NYC.⁸⁸³ However, the signatory states have the discretion to not be bound by this provision.

5.5.1 *Arbitrable matters*

In most countries, compensation or interest for late payment is allowed, with differences in the laws and practices, whether for late payment or for actual damages, as previously mentioned (see Chapter Four). Commercial claims are often arbitrable in most countries, even within the Arab and Islamic countries, but claims including illegal interest or usury can be very complicated, as examined above. This is especially the case in countries that do not distinguish between substantive and procedural rules with respect to interest.

As stated, interest usury claims are not arbitrable under French law. An award containing usury may be considered as non-enforceable as such an award may be seen as breaching international public policy (see Chapter Four). In the U.S., under some state laws, illegal interest or usury is non-arbitrable under the law of arbitration seat; therefore the courts would refuse to enforce the award if it is contrary to the state usury law or public policy.⁸⁸⁴ In England, no mention of non-arbitrable matters is made⁸⁸⁵ based on party autonomy, a practice allowed by the English Arbitration Act. However, such autonomy is subject to unreasonable terms and public policy.

In *Sharia* law, some types of interest such as *Riba* are considered non-arbitrable as mentioned above. However, not all interest is non-arbitrable (see Chapters Three and Four). In fact, such matters would be unenforceable rather than non-arbitrable under *Sharia* law and public policy. Under the Saudi Arbitration law, disputes related to commercial matters are arbitrable and the award will be enforced unless it is contrary to *Sharia*. Thus, a foreign arbitral award that contains *Riba* or an interest-based loan is unenforceable. Similarly, the Egyptian Civil code allows the parties to agree to the interest rate and pay interest for the late payment.⁸⁸⁶ However, if the contract is subject to Egyptian law, the usury or illegal interest would not be enforced under its law according to public policy (see Chapter Four).

⁸⁸³ See Born (n 22) 567,1501 'To the same effect is Article II(1) of the Convention, providing exceptionally for non-recognition of arbitration agreements in a particular Contracting State as to matters defined as non-arbitrable under local mandatory law.'

⁸⁸⁴ *Party Yards, Inc. v. Templeton*, 751 So. 2d 121 (Fla. Dist. Ct. App. 2000) 'held that a usury violation is not arbitrable; it is a matter for the courts'. See Chapter Four and Five.

⁸⁸⁵ The Arbitration Act, 1996, does not define arbitrability, which is determined under the Common Law and the approach to "arbitrability is very broad and only excludes disputes that would affect the public at large, see Vorburger 35-82.

⁸⁸⁶ As mentioned before in Chapter Three, Act 227(1) of the Egyptian Civil Code 1949 "The contracting parties can agree on a different rate of interest, whether in return for a delay in payment or in any other situation, on condition that this rate does not exceed 7 per cent. If they agree on an interest that exceeds this rate, this interest will be reduced to 7 per cent, and any surplus already paid must be returned." And Act 226 of the same code, for more info also see Larry A DiMatteo, *International Sales Law: A Global Challenge* (Cambridge University Press 2014) 513.

Gemmell and Kutty observe that with regards to the recognition and enforcement of foreign arbitral awards in Islamic countries such as Saudi Arabia, Egypt, and the UAE, the awards may be subject to compliance with *Sharia*.⁸⁸⁷ For instance, in the case of the UAE, civil loan contracts and compound interest should not be allowed under the *Sharia*.⁸⁸⁸ However, it is worth noting that it is debatable whether compound interest is in practice allowed or not.⁸⁸⁹ In contrast, the law allows charging of simple interest on loan contract,⁸⁹⁰ according to the interpretation that it is an economic necessity,⁸⁹¹ despite the fact that such interest is contrary to *Sharia* law (see Chapter Four). Furthermore, civil loan claims subject to UAE law are deemed non-arbitrable.⁸⁹²

5.5.1.1 Punitive damages

Punitive damages may be considered non-arbitrable according to some laws under the court in the place of enforcement when related to the awarding of interest. Similar to bankruptcy matters affecting the enforceability of the arbitration agreement as non-arbitrable under Art V (2) (a),⁸⁹³ punitive damage can be non-arbitrable as it may affect the enforceability of the award. However, as discussed, the non-arbitrability of punitive damages is subject to debates due to the different interpretations given by the systems of Civil Law and Common Law. Accordingly, this issue depends on whether the parties have agreed or not, whether they have chosen a law governing their contract or not, and whether the punitive damages are related to substantive or procedural issues. In the U.S. the damages would not be enforced if contrary to public policy,⁸⁹⁴ likewise the approach of most countries if they are related to usury or substantive issues. Furthermore, if the punitive clause is strongly prejudicial to the other party,⁸⁹⁵ or is contrary to the law applicable to the contract, it is non-arbitrable under such law (see Chapter Four). In contrast, the U.S. courts rule in favour of arbitration if the parties have agreed with regards to

⁸⁸⁷ Gemmell (n 114)187; Kutty (n 25) 67.

⁸⁸⁸ Act 4 of the Civil Courts Procedures Law

⁸⁸⁹ See See Tamini 50; see also Kanakri 217–255.

⁸⁹⁰ In Arts 76 and 77 of Federal Commercial Transactions Law, which must not exceed 12% per annum in commercial matters and 9% for non-commercial matters, Arts 76 and 77 of Federal Law 18 of 1993 that asserted provisions of Articles 61 and 62. For e.g. see *Airmech Dubai LLC v. Maxtel International LLC*, *Court of Cassation of Dubai*, Appeal No. 132 of 2012, 18 September 2012 in Jalal El--Ahdab (ed), 'International Journal of Arab Arbitration' (2013) 5(1) International Journal of Arab Arbitration, 56; See the judgment of the Federal Supreme Court of Abu Dhabi 245/20 of May 7 2000

⁸⁹¹ See Mistelis and Brekoulakis 293–316. 'Given the express statement of the Law and the Interpretative Decision No. 14/9 (28 June 1981) of the Constitutional Department of the Federal Supreme Court of Abu Dhabi (economic necessity requires the charging of simple interest by banks), ... disputes as to simple interest must be presumed as arbitrable in the UAE'.

⁸⁹² See Chapter Four.

⁸⁹³ Born (n 22) 613.

⁸⁹⁴ See *Laminoirs-Trefileries-Cableries de Lens SA v Southwire Co*, 484 F Supp 1063 (ND Georgia 1980) 'US Federal District Court refused to enforce a foreign arbitral award under the New York Convention on public policy grounds because the arbitrators' increase of interest rates by an additional 5% would amount to punitive damage and would not be enforceable'; see also *Bridge Fund Capital Corp v Fastbucks Franchise BT - F 3d* (2010) 622 996 [999-1003]

⁸⁹⁵ Ben-Shahar 869.

punitive damages.⁸⁹⁶ Thus, it is ‘a private process to which the parties have agreed, and the courts’ only obligation is to uphold that agreement pursuant to established arbitration and contract law’,⁸⁹⁷ where ‘the case law reveals that the clear trend is to empower arbitrators to award punitive damages’.⁸⁹⁸

However, under the agreement of the parties, the arbitrators have the authority to award punitive damages.⁸⁹⁹ Although the parties may give the arbitrator a general authority to settle the dispute as it deems appropriate, it may reject an award in case the parties have not expressly agreed upon punitive damages. However, ‘the majority position is now that contracting parties have the right to authorize to award punitive damages and, impliedly, such authority is part of the arbitral tribunal’s general mandate which does not need not be expressly conferred by the parties’,⁹⁰⁰ unless the parties otherwise agreed.⁹⁰¹ In case the parties do not agree on such matter, the applicable law to the contract determines the legality of the punitive damages under different approaches.

Although punitive damages may be allowed and arbitrable under the law applicable to the contract, they may still be rejected under the law of the enforcing court. Some countries may consider such matter as non-arbitrable or unenforceable if it is contrary to substantive laws or public policy, otherwise it is arbitrable,⁹⁰² even if the award is valid under the law applicable to the dispute, or arbitrable under the seat of arbitration. Other countries would consider punitive

⁸⁹⁶ The U.S. Supreme Court in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 63 U.S.L.W. at 4195 (1995), held “... we have previously held that the FAA’s pro-arbitration policy does not operate without regard to the wishes of the contracting parties.”... “The Court found that the rules incorporated in the contract allowed punitive damages, thus at most, the New York choice-of- law provision introduced an ambiguity into the contract, which should be resolved in favour of arbitrating the punitive damages issue”; In *Volt Information Sciences, Inc. v. Board of Trustees of the Leland Stanford Junior University*, 489 U.S. 468, 478-479, 109 S. Ct. 1248, 1255, 103 L.Ed.2d 488 (1989), the Supreme Court held that the “parties are generally free to structure their arbitration agreement as they see fit.” The federal district court in *Willis v. Shearson/ American Express Inc.* 569 F. Supp. 821 (M.D.N.C. 1983), held that a claim for punitive damages was arbitrable due to there was no “public policy reason persuasive enough to justify prohibiting arbitrators from resolving issues of punitive damages submitted by the parties”.

⁸⁹⁷ Charles Smith, *The Application of Due Process to Arbitration Awards of Punitive Damages—Where is State Action?*, 2007 J. DISP. RESOL. 417, 419.

⁸⁹⁸ Stephen P Bedell, Mary Beth Cyze and Donn M Davis, ‘Current Developments in Arbitration: Arbitrability and Punitive Damages, 22 J. Marshall L. Rev. 603 (1989)’ (1989) 22 The John Marshall Law Review 4, 4.

⁸⁹⁹ See Mistelis and Brekoulakis 224; see also Chernick, Kolkey and Neal 113.

⁹⁰⁰ Thomas E Carboneau, *Carboneau on Arbitration: Collected Essays* (JurisNet 2010) 368.

⁹⁰¹ Farnsworth 93 ‘If the arbitration clause plainly stated that the arbitrators have no power to award punitive damages, that ends the matter – in every jurisdiction, even where arbitrators would otherwise have that power.’

⁹⁰² Such as Saudi Arabia, where Sharia law does not allow to agree on punitive damages with regards to late payment, unless there is actual damages, but allow to agree on punitive damages with regards to breach of contracts (see Chapter Four). Likewise United States, where the punitive damages with regards to usury is contrary public policy and the substantive law (see Chapter Four). However, punitive damages with regards to breach of contract is allowed under the federal law, under the place of enforcement. Although such matter is different from one state to another. Thus, override the maximum limitation of compensation or interest more than actual damage or the punitive is considered against the rules of justice and public policy in California law, where it is conflict with the Texas’ law and public policy (see Chapter Four and Six). See e.g. *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d.*

damages as arbitrable and leave such matter to the parties and arbitrators unless the award is contrary to public policy,⁹⁰³ or the law applicable to the dispute has implied level of interest.⁹⁰⁴

However, contracting States to the Act shall only treat specific subjects as non-arbitrable on an exceptional basis, in order to further discrete, articulated public policies. A state must exercise self-restraint and avoid generating a broad category of issues defined as non-arbitrable.⁹⁰⁵

5.5.1.2 Separability of arbitrable and non-arbitrable in an award

In principle, the court of the enforcement place should not review the merits of the dispute of the award.⁹⁰⁶ However, all signatory countries to the NYC exercise different levels of review, either procedurally or substantively. Consequently, the national courts may reject the enforcement the foreign arbitral award that contains illegal interest which is disallowed under their national law or public policy. However, some of these countries would apply the principle of separability with regards to the violation part of the award and only reject the non-arbitrable part of the award.⁹⁰⁷

5.5.2 *Arbitrability of the arbitrable*

A legal conflict could arise where the NYC enables a contracting State the discretion to consider and refuse enforcement of an award which deals with non-arbitrable matters under under Art V (2) (a) regarding the subject matter of the dispute. This has similar effects as those under Art (II) (1). According to Born,

‘the effect of Articles V (2) (a) and II (1) is to permit individual Contracting States to impose limits on the enforceability of international arbitration agreements, notwithstanding the validity of such agreements under the Convention and applicable law’.⁹⁰⁸

Thus, such matter can be considered twice, once under the law of the arbitration seat and once under the law of the enforcement country. Indeed, the subject matter of dispute with regards

⁹⁰³ Such as France, where the punitive damages are arbitrable unless the award is contrary to the international public polic (see Chapter Four).

⁹⁰⁴ Such as England, where under its law it does not allow awarding punitive damages unless there is an actual damage, and the implied interest will be applied if there is no agreement under the Sale of contract Act under the Late payment Act (see Chapter Four). Likewise Egypt where its law is applies impelidly to the awarding of punitive damages, where reject enforcement interest that is higher than the allowable rate. UAE law is only applied in case the punitive damages related to the loan contract (see Chapter Four and Six)

⁹⁰⁵ Born (n 22) 614.

⁹⁰⁶ see Redfern 450; see also Born (n 22) 3025. In Saudi Arabia, the merits of dispute should not be reviewed by the courts, see royal order No. 7260 dated 03/21/1433 AH, which was issued two months before the Saudi Arbitration Law 2012.

⁹⁰⁷ In Saudi Arabia, the arbitral award is binding unless it is contrary to Sharia law or public policy such as the issue Riba, where the violation part of the award will not be enforced. See Chapter three, See the case No 269/Es 4 of 1431H in 2011, where the court overturned a part of an ICC award containing usury which was defined as contrary to public policy and Sharia law, see Art 55 of the Saudi Arbitration Law see also Art 9 and Art 11 (4) of the Saudi enforcement law, No 13/T 4892 on 28/02/2013. Likewise, the Egyptian practise, where reject only the illegal interest under the its law.

⁹⁰⁸ See Born (n 22) 566.

to non-arbitrability is reconsidered three times, under Art II (1), under Art V (1) (c) and under Art V (2) (b) as mentioned previously, outlining arbitrability of the arbitrable. Logically, to avoid the issues being examined at different stages of arbitration by different courts, it is best to allow the enforcing court to take the sole task under Act V (2) (a) since it has direct interest in the outcome of the enforcement of the award.

5.5.2.1 Arbitrability and public policy

Public policy and arbitrability are interrelated and inseparable; thereby, some jurisdictions may refer to both terms as previously mentioned. However, most courts' justifications and arguments regarding non-arbitrable matters are based on a violation of public policy.⁹⁰⁹ It is important to distinguish between arbitrability in general and public policy, though they share many common characteristics with each other. According to various interpretations, the direct non-arbitrable matters under Art II (1) and Art V (2) (a) are related to the substantive public policy with regards to the merits of dispute concerning illegal interest rates or usury. Indirect non-arbitrability is related to both the substantive and procedural public policy regarding to contract with respect to the invalidity of the arbitration agreement under Art II (3) and Art V (1) (a). In addition, Art V (1) (c) and (e) are related to either the substantive or the procedural public policy under different interpretations.

5.6 Conclusion

The law applicable to the dispute is the law determining the legality of interest (usury in loan contract, late payment, compensation and damages) and the legality of the parties' clauses in this regard. In the absence of such a choice, the matter is left to the arbitrators to determine their jurisdiction, the applicable law or the scope of the arbitration and the dispute, and the authority to award interest. The law of the arbitration seat is the law implied into this issue under Art V(1)(c) of the NYC. The national arbitration law of the arbitration seat would apply automatically, either by parties' agreement or by tribunal's choice of place of arbitration, under some arbitration seats. Such application should only be made where no choice of law agreement was made.

A valid agreement to arbitrate may contain some general terms such as the choice of law, place of arbitration etc. or may merely refer to arbitration. Such a submission may include specific terms such as the determination of interest rate and the time period. The parties cannot rely on the scope of the arbitration as a ground for refusal in all cases when a link between the disputes and

⁹⁰⁹ See Born (n 22) 6, 606, 3786; Chernick, Kolkey and Neal 113, 945; see also Mistelis and Brekoulakis 169, 285, 341.

contract can be made and where there is an arbitration agreement manifesting the parties' wishes to subject their disputes to arbitration. The scope of arbitration is determined under the arbitration agreement, which provides arbitrators with the authority and the power, whether general or specific, and whether the law is expressly or implicitly applicable. Under the arbitration agreement, the arbitrator gains his authority to award interest, whether such interest rate is expressed or implied under the applicable law. The arbitral award can also be subjected to the applicable law, by the parties' agreement if no appropriate choice was made by the parties. Awarding interest should not be considered as a punitive damage where there is an agreement or under the general authority of the arbitrator. Awarding interest should be considered within the scope of arbitration and dispute in loan, late payment, compensation, etc. or any type of contracts related to interest. An arbitration agreement may refer to a dispute that has arisen or will arise.

Although the interest law can be subject to the law applicable to the contract if the parties have chosen such law expressly or impliedly, the potential application of different interest laws may negatively affect to arbitrability, whether they are the laws of the arbitration seat, the laws applicable to the contract or the laws of the enforcing court. The reading of Articles I and V of the New York Convention, which require no substantive review of awards, seems not to be followed in this subject in terms of the recognition and enforcement of arbitration agreement and awards. The concept of arbitrability in relation to interest disputes encounters different laws and interpretations, which frustrate the purpose of the New York Convention which was intended to ensure the enforceability of foreign arbitral awards. It is the researcher's viewpoint that the Convention should be interpreted in favour of arbitration, according to the nature of arbitration and the party autonomy. Non-arbitrable matters shall only cover those matters that require governmental approval or are fundamentally non-arbitrable. Neither interest claims nor awarding interest should be considered non-arbitrable. In addition, such a matter should not be reviewed twice, under the seat of arbitration and again under the enforcement place.

An arbitration agreement is binding unless it is clearly invalid or voidable, whether in a separate agreement or an arbitration clause. An award is binding under a valid agreement unless the subject matter of the award is non-arbitrable or the award is contrary to public policy in the eyes of the enforcing court. However, conflicts may arise from the imposition of the law of the arbitration seat, the applicable law to the dispute or the contract and the law of the country of enforcement, in terms of the finality of an award. This potential conflict will not fit into any useful legislative purpose and further frustrates the parties' purpose in choosing arbitration to resolve their disputes. Such conflicts in approaches lead to undesirable different interpretations and ambiguities between public policy and non-arbitrability, as this chapter has proven. The principle of public policy has been taken into account by these countries in many places under the seat of arbitration under Art V(1)(e), and under the enforcement place according to Art V (2)(a) and Art

V (2)(b). The combination of public policy and national law may have negative impacts on the merits of disputes with regard to interest and the determination of non-arbitrable matters. However, as stated above, non-arbitrable matters should be applied narrowly under Art II (1) and a clear distinction between Art V (2) (a) and Art V (2) (b) should also be made, as non-arbitrability should not be interpreted in the same way as the meaning of public policy.

Chapter 6. Public policy and enforceability

6.1 Introduction

There are many obstacles and constraints that may affect the arbitration process, the nature of arbitration and its purpose. The interpretation of the conventions, conflict of laws, determination of the procedural and substantive rules, and judicial review all have a direct impact on enforcement of foreign arbitral awards. Public policy is one of the grounds for setting aside or refusing foreign arbitral awards according to Art V 2(b) of the NYC, Art 36 (2) and Art 34 of the UNCITRAL Model Law, and the Saudi Arbitration law. This is an acute issue in terms of enforcement of an award containing *Riba*, especially when no clear definition of public policy was offered under these conventions and arbitration laws. Individual interpretations of public policy under different courts would lead to create uncertainty about the fate of the enforcement of international arbitral awards and diminish the value of the NYC. Such interpretations would inevitably cause more disputes between states, especially in those countries where public policy is not clearly defined, and would disrupt the function of arbitration. The intervention of national courts in the enforcement of the arbitral award regarding public policy has increased, but there is a desire to release arbitration from the grip of the courts in these cases.⁹¹⁰

The concerns over public policy lie in two parts: when the State gives a broad interpretation of public policy and when this interpretation is applied by the national courts.⁹¹¹ In this chapter, the concept and limits of public policy will be identified first before a discussion of different types of public policy is made. The thesis will further articulate the relationship between law and public policy and conclude with a view on how the issue of usury and interest shall be addressed.

6.1.1 The public policy concept

Public policy, by its nature, is a dynamic concept that evolves continually to meet the changing needs of an individual society, including its political, social, cultural, moral, and economic dimensions,⁹¹² but 'defining public policy is a hard and complicated task'.⁹¹³ Public

⁹¹⁰ Christopher S Gibson, 'Arbitration, Civilization and Public Policy: Seeking Counterpoise between Arbitral Autonomy and the Public Policy Defense in View of Foreign Mandatory Public Law' [2009] Penn State Law Review, Forthcoming.

⁹¹¹ Karl-Heinz Bockstiegel, 'Public Policy and Arbitrability' in Pieter Sanders (ed), *Comparative Arbitration Practice and Public Policy in Arbitration* (Kluwer Law International 1987) 189.

⁹¹² Mistelis, 'International Law Association-London Conference (2000) Committee on International Commercial Arbitration Keeping the Unruly Horse in Control or Public Policy as a Bar to Enforcement of (Foreign) Arbitral Awards' 252.

⁹¹³ The Court of Appeal of Lisbon, see Duarte Gorjão Henriques and BCII Advogados, 'National Mandatory Rules and International Public Policy: The Status of the Agent's Goodwill Compensation in Portugal' (*Kluwer Arbitration Blog*, 2014) <<http://klowerarbitrationblog.com/blog/2014/04/25/national-mandatory-rules-and-international-public-policy-the-status-of-the-agents-goodwill-compensation-in-portugal/>> accessed 12 October 2015.

policy allows the judicial system to protect public interests in cases of disputes and enforcement of awards. This defence has been frequently used in contracts to which the State is a party. Public policy is a functional concept and so it is particularly difficult to give a uniform definition. Some judges and authors describe public policy as 'a very unruly horse, and when once you get astride it you never know where it will carry you'.⁹¹⁴ Consequently, public policy is more than a law provision; it is an on-going process, a complex concept and that isn't a specific fixed notion as 'it is impossible to say what the opinion of a man or a judge might be as to what public policy is'.⁹¹⁵ However, a search through international practices may guide us toward the meaning of public policy. An attempt made by the House of Lords of England in 1853 found that: 'public policy, through understanding its purpose, does not allow doing anything, which would harm the main principles of any community',⁹¹⁶ and indicated that morality and the basic principles of law and fundamentals of justice served as good guidance to what may constitute public policy. Similarly, the main source of law is also an indicator of public policy. Contractual terms that are against public policy are unenforceable under Common Law. Common Law might not include all violations of procedural cases⁹¹⁷ but it does for violations restricted to substantive cases.⁹¹⁸ Hence, there are differences between the concept of public policy in Common Law as well as Civil Law, which is discussed later.

Zekos argues that public policy can be identified as: mandatory laws, fundamental principles of law, public order, good morals, national interests and foreign relations.⁹¹⁹ Some countries interpret public policy based on principles of justice, others through understanding the basics of a social policy. In Russia, the Supreme Court interprets public policy through understanding the basics of the social policy of the Russian Federation, and this interpretation can be applied in individual matters. With the Russian-oriented social policy serving as one of the indicators of what constitutes a breach of public policy as applied by the Russian courts, the enforcement of a foreign arbitral award against such policy would result in an unacceptable consequence and potential negative result for Russian society, so the subject is extremely complex.⁹²⁰ The German courts have a narrow interpretation based on the fundamental concept of justice in Germany for public policy, which is based on a narrow interpretation of principles of justice and

⁹¹⁴ *Richardson v Mellish BT - Bing* (1824) 2 229 [252]; *Mogul Case BT - AC* (1892) 1892 25 [Lord Bramwell].

⁹¹⁵ See *Besant v Wood BT - Ch D* (1879) 12 605; cited in *Penunuri v Sundance Partners, Ltd BT - P 3d* (2011) 257 1049 [1054].

⁹¹⁶ *Egerton's Case BT - HLC* (1853) 4 1.

⁹¹⁷ Aron Broches. *Commentary on the UNCITRAL Model Law on International Commercial Arbitration* (Springer Netherlands 1990) 191.

⁹¹⁸ Pieter Sanders, TMC Asser Instituut and International Council for Commercial Arbitration, *Comparative Arbitration Practice and Public Policy in Arbitration* (Kluwer Law and Taxation Publishers 1987) 179.

⁹¹⁹ Zekos 44-45.

⁹²⁰ See the Decree of the Presidium of the Supreme Court of the Russian Federation of 25 September 1998, Bulletin of the Supreme Court of the Russian Federation, n°3, 1999, p.13.

a violation of the public policy in Germany in accordance with foreign arbitral awards exists only when the award is contrary to the rules that are basic in public or commercial life in Germany, or when it is contrary to the fundamental concept of justice of Germany.⁹²¹

Thus, the violation of the procedural or substantive rules by the arbitrator is not enough to apply the principle of public policy by the courts. In the U.S. in 1974, Judge Joseph Smith stated that a foreign arbitral award might be rejected based on public policy only if the awards 'violate the forum state's most basic notions of morality and justice'.⁹²² To what extent such conflicts would be between different legal systems, where these principles would lead to more conflicts with regards to usury and its interpretation in a larger scale, and whether this is considered violation to public policy or not, is key to understanding the issue.

The New York Convention does not provide any guidance on the interpretation of public policy. Public policy has been described as 'multi-faceted',⁹²³ 'open-textured and flexible'⁹²⁴ with 'various guises' and therefore having a 'great diversity in the vocabulary and ambiguities'.⁹²⁵ The legislatures and courts are, understandably, reluctant to define public policy exhaustively.⁹²⁶ Public policy has many definitions with a common relation between them, which can show the link between the law or legislative power and the general meaning of public policy, but the definition is still loose and can be affected by time and place.

Some scholars define public policy as a framework of 'regulatory measures, courses of action, laws, and funding priorities with regard to a given topic issued by the authority or its delegates'.⁹²⁷ In general, public policy is a law containing certain legislation and provisions of constitutional or international law.

6.2 The public policy types

According to different interpretations and scopes, public policy has several categories, such as national, international and transnational public policy. Such categories are applied by different countries, whether by referring to the concept or interpretation of public policy.

⁹²¹ BGH. 12 July 1990 – III ZR 174/89. NJW 1990, 3210.

⁹²² *Parsons & Whittier Oils Co., Inc v Societe G. DE L. DU P. (R) BT - F 2d* (1974) 508 969 [974].

⁹²³ *Hebei Import & Export Corp v Polytek Engineering Co. Ltd* [1999] 1 HKLRD 552 (Hong Kong Court of Final Appeal, 9 February 1999)

⁹²⁴ *Renusagar Power Co Ltd v General Electric Co*, Supreme Court of India, 7 October 1993, extract in Yearbook Commercial Arbitration XX (1995, India No. 22) [26]. Available in Albert Jan van den Berg (ed), 'Yearbook Commercial Arbitration 1995 - Volume XX' (1995) 20 Yearbook Commercial Arbitration 681.

⁹²⁵ Yves Derains, 'Public Policy and the Law Applicable to the Dispute in International Arbitration' in Pieter Sanders (ed), *Comparative Arbitration Practice and Public Policy in Arbitration* (Kluwer Law International 1987) 228.

⁹²⁶ In *Deutsche Schachtbau- und Tiefbohrgesellschaft mbH v Ras Al Khaimah National Oil Co and Shell International Co Ltd* [1987] 2 Lloyd's Rep 246, per Donaldson MR. In *Wilkinson v Osborne* (1915) 2 CLR 89, 97, per Lord Isaacs.

⁹²⁷ See Reviews, C. T., 2012, e-Study Guide for: Business Law and the Legal Environment, Standard Edition by Jeffrey F. Beatty; Schuster, W. Michael. For the Greater Good: The Use of Public Policy Considerations in Confirming Chapter 11 Plans of Reorganization (December 31, 2008). Houston Law Review, Vol. 46, p. 467, 2009.

6.2.1 *International public policy*

The International Law Association (ILA) defines ‘international arbitral awards’ as awards ‘which are not strictly domestic and which include a material foreign element’.⁹²⁸ Some think that international public policy covers public interest concerns that exist among different nations, and that this would lead to the easy enforcement of the foreign award. This would overcome confusion due to national elements related to the residence and business place of the parties, and the subject of arbitration or dispute of these parties when the two are from different countries.⁹²⁹ The public policy of transnational or truly international laws denotes those fundamental rules of natural law, rules of international justice, peremptory norms and common rules of morality that are admitted by civilised countries.⁹³⁰ There are some considerations toward the concept of international public policy in the practice of private international law as it is applied in some countries, such as France. International public policy is considered as a general policy in the sense of private international law.⁹³¹ However, the lack of definition fails to convince many countries of the viability of this concept, which is rooted in confusion over its interpretation and in the application of public policy.

There are those who believe that national public policy in common forms part of international public policy,⁹³² but international public policy remains narrower than most domestic public policy.⁹³³ This may be due only to considerations of international or regional conventions and international substantive and procedural rules, and not to domestic procedural and substantive rules or national laws. In addition, the word “international” in the concept of international public policy also means it is a subject within the scope of private international law,

⁹²⁸ ILA Report 250. See Recommendation 1(c) of ‘Report on Public Policy as a Bar to the Recognition and Enforcement of International Arbitral Awards’ (2002).

⁹²⁹ Mistelis and Brekoulakis 12–13.

⁹³⁰ Mark A Buchanan, ‘Public Policy and International Commercial Arbitration’ (1988) 26 *American Business Law Journal* 511, 511; ILA Final Report 259; Julian Lew, *Applicable Law in Commercial Arbitration: A Study in Commercial Arbitration Awards* (1978) 534–535 Para 407; Okezie Chukwumerije, *Choice of Law in International Commercial Arbitration* (1994) 192; Domenico Di Pietro and Martin Platte, *Enforcement of International Arbitration Awards: The New York Convention of 1958* (2001) 181–182.

⁹³¹ AN Zhilsov, ‘Mandatory and Public Policy Rules in International Commercial Arbitration’ (1995) 42 *Netherlands International Law Review* 81, 97.

⁹³² Lew, Mistelis and Kroll 723; Buchanan 511–14, 530; Pierre Lalive, ‘Transnational (truly International) Public Policy and International Arbitration’ (1986) VIII *International Congress on Arbitration* 258.

⁹³³ See ILA Final Report 252; Christopher Kuner, ‘The Public Policy Exception to the Enforcement of Foreign Arbitral Awards in the United States and West Germany Under the New York Convention’ (1990) 7 *Journal of International Arbitration* 71, 89–90; Loukas Mistelis, ‘Keeping the Unruly Horse in Control or Public Policy as a Bar to Enforcement of (Foreign) Arbitral Awards’ (2000) 2 *International Law Forum Du Droit International* 248, 250–251; Hrvoje Sikiric, ‘Arbitration and Public Policy: Arbitration proceedings and Public Policy’ (2000) 7 *Croatian Arbitration Yearbook* 85, 87; Philip Daniels, *Analyse the Role of Public Policy as a Ground for Opposing Recognition and Enforcement of International Arbitration Awards in the New York Convention and Model Law* (LLM Thesis, University of Queensland, 1994) 18; Albert Jan van den Berg, *The New York Arbitration Convention of 1958: Towards a Uniform Judicial Interpretation* (1981) 360; Andrew Okekeifere, ‘Public Policy and Arbitrability under the UNCITRAL Model Law’ (1999) 2 *International Arbitration Law Review* 70, 70–71; AN Zhilsov, ‘Mandatory and Public Policy Rules in International Commercial Arbitration’ (1995) 42 *Netherlands International Law Review* 81, 97.

falling in the scope of commercial transactions with a foreign party.⁹³⁴ There are ambiguities with respect to the terms 'international' or 'transnational' when associated with public international law. The clearer choice is 'international' because it applies to transactions that have connections with other countries. International public policy is different from transnational public policy because it does not aim to be 'genuinely international',⁹³⁵ 'truly international',⁹³⁶ and 'really international'.⁹³⁷

However, the concepts of international public policy and national public policy are inevitably overlapped with each other within the area of law. The rules of national public policy may be reflected in the rules of international public policy. The principles of freedom of the parties, good faith and other principles of law may represent categories of international public policy as internationally agreed. Nonetheless, it is not necessarily the case that other principles, such as principle of justice, would be considered part of international public policy. Therefore, international public policy cannot be part of national policy in all aspects, but only some, and it cannot determine or constrain these rules selectively. In this case the national public policy is more important than the international public policy because it is in the interests of the State.

In France, it seems the interpretation of international public policy is narrower than that for the national, and international public policy does not contain every part of the national public policy.⁹³⁸ Therefore, the conception and application of international public policy are still inoperative in France, and it cannot be shown that France is trying to give a definition and apply a common international standard. However, the international public policy is applied in France, but disputes regarding interest are still unclear and unpredictable. International public policy is understood to be narrower than domestic public policy: not every rule of law which belongs to the *ordre public interne* is necessarily part of the *ordre public externe* or *international*. Professor Sanders states 'international public policy, according to a generally accepted doctrine is confined to violation of really fundamental conceptions of legal order in the country concerned'.⁹³⁹ However, 'until now, has been able to suggest a definition of 'international public policy' that could enable a judge to solve any given dispute without hesitation'.⁹⁴⁰

⁹³⁴ Hans van Houtte, 'From a National to a European Public Policy' in James Nafziger and Symeon Symeonides (eds), *Law & Justice in a Multistate World – Essays in Honour of Arthur T Von Mehren* (2002) 841, 884.

⁹³⁵ See Mistelis and Brekoulakis 12–13; see also Savage and Gaillard 853–863.

⁹³⁶ Born, *International Commercial Arbitration*; Mistelis and Brekoulakis; Alan Redfern, J Martin Hunter and Nigel Blackaby Constantine Partasides, *Redfern and Hunter on International Arbitration* (Alan Redfern and others eds, 5th editio, Oxford University Press 2009) <<http://www.kluwerarbitration.com>>; Savage and Gaillard 738.

⁹³⁷ Savage and Gaillard 863.

⁹³⁸ See Albert Jan van den Berg, 'Distinction Domestic-International Public Policy, New York Consolidated Commentary Cases' (1996) XXI ICCA Yearbook 502; see also 'Report on Public Policy as a Bar to the Recognition and Enforcement of International Arbitral Awards' 3; Albert Jan van den Berg, *The New York Arbitration Convention of 1958: Towards a Uniform Judicial Interpretation* (1981) 268.

⁹³⁹ Sanders, 'Commentary' in *60 Years of ICC Arbitration - A Look at the Future* (ICC Publishing, 1984).

⁹⁴⁰ See Henriques and Advogados.

Linking usury and interest with public policy can be further complicated to this this lack of definition in international public policy and different views expressed by the national courts on the subjects of usury and interest. Usury and interest issues vary from one law to another, which means that they may pose a dilemma when applying the concept of international public policy. There is no unified reliable international law with regard to usury or interest in order to apply the concept of international public policy. French law clearly indicates that usury is forbidden,⁹⁴¹ and France limits the choice of law to mandatory laws if the enforcement of the award would breach international public policy of the seat or lead to a breach of public policy.⁹⁴² France uses the concept of international public policy constantly in enforcement of arbitral agreements on the choice of the law and in the enforcement of the arbitral award. In case of a dispute which involves a foreign element, France applies the principles of private international law to determine the substantive law governing the dispute. The court will see that mandatory rules are neither considered '*lois de police*' nor breaches of the international public policy in international arbitration.⁹⁴³ The Court of Appeal in Paris⁹⁴⁴ has held if the interest rates do not exceed the threshold of usury in foreign jurisdictions, it would not constitute a violation of French international public policy, which means the acceptance of interest rates in foreign jurisdictions. Usury is a violation of substantive law in France under both French law and in domestic arbitration, but in international commercial arbitration it is not unless the maximum interest rates breach a foreign law. Thus, it should not exceed the substantive law for usury or the illegal interest rates in the foreign State due to the concept of international public policy. To what extent such theory would be applied if the parties have chosen *Sharia* as the governing law of their contract, even only with 1% as the threshold of usury remains unclear, also affecting decisions over rates, period, compensation and punitive damage in breaches of contract or tort, under various interpretations.

6.2.1.1 The problems of applying international public policy

The international public policy is based on different philosophies, one of those being that international arbitrators when working within the concept of international public policy should decide their judgments in accordance with the values widely accepted by the international community and at their own discretion, even when having an impact on national public policy.⁹⁴⁵ Neither French law nor ILA give a clear definition for the international public policy. The

⁹⁴¹ Law No. 93-349 of July 26, 1993, as Article L. 313 et seq. of the French Consumer Code, see 'Conflict of Laws in International Loans to French Corporations: The Usury Question' (2008).

<<http://corporate.findlaw.com/finance/conflict-of-laws-in-international-loans-to-french-corporations.html#sthash.ae1JXo4y.dpuf>> accessed 11 October 2015.

⁹⁴² See Bars and Kaminsky.

⁹⁴³ Cass. Com., November 28, 2000, Allium.

⁹⁴⁴ *Holding Company Iro-v. Sétilex Society*, C.A. Paris I, June 9, 1983, in *Journal of arbitration* 1983, p. 497.

⁹⁴⁵ Savage and Gaillard 853.

application of international public policy is only one exception, where there are no unified rules or laws regarding interest etc. on the international scale. ILA 2002 ratified the narrow approach to public policy – a refusal to implement under the public policy exception in exceptional circumstances only, where such international public policy is a set of principles and rules recognized by the state, to seek to facilitate the final decisions of the arbitration in accordance with the main objective of facilitating the enforcement of arbitral awards under the NYC. Moreover, ILA referred to the justice or morality that should be protected by the State to serve political, social or economic interests. It referred indirectly to the law, where a law protects such matters. On the other hand, it is not possible identify the rules of justice on an international scale when they vary from one nation to another, and the concept of public morality cannot be applied on an international scale.

ILA tried to get out of this impasse by attempting to think of reasons for rejection of enforcement. It seems that the ILA was not sure or clear about rules of international public policy, they could not even define international public policy and sought to rely on the finer details of the refusal to identify international public policy. The lack of reliance on Art V (2)(b) is due to distrust of it being a general concept that cannot be used to determine requirements to clarify the concept of public policy and also over general confusion in this concept. The methodology applied by the ILA also sees conflicting court judgments on this matter, which makes it difficult to conclude an optimal definition of the international public policy. However, the state's duty is to respect its obligations to other states with respect to the application of the NYC within the concept of public policy and without further interpretations.

The principle of separability of arbitration agreements examined in Chapter Five is one of the solutions that is proposed by the ILA,⁹⁴⁶ but again it is not possible to identify the part that does not conflict with international public policy. More consideration was given to the principles of law, whether procedural or substantive.⁹⁴⁷ In the U.S., in *Laminoirs- Trefileries-Cableries de Lens, S.A. v. Southwire Co.*, a U.S. court refused to enforce part of the arbitral award that was contrary to public policy, which was required payment of a usurious interest rate.⁹⁴⁸ In this case

⁹⁴⁶ The International Law Association stated; 'If any part of the award, which violates international public policy can be separated from any part which does not, that part which does not violate international public policy may be recognised or enforced'. See the 70th Conference of *International Law Association on Public Policy as a Bar to Enforcement of International Arbitral Awards*, held in New Delhi, India, 2-6 April 2002. 1 H

⁹⁴⁷ It was stated; 'the court must ensure that the arbitration award is matching with the fundamental principles, whether procedural or substantive. It must be done by reference to those principles that are considered fundamental within its own legal system, and not in the context of the law governing the contract or the law of the place of enforcement, or the law of the seat of arbitration'. The 70th Conference of *International Law Association on Public Policy as a Bar to Enforcement of International Arbitral Awards*, held in New Delhi, India, 2-6 April 2002.

⁹⁴⁸ *Laminoirs-Trefileries-Cableries de Lens, S.A. v. Southwire Co.*, 484 F. Supp. 1063, 1069 (N.D. Ga. 1980). Laminoirs, a French company, agreed to manufacture and sell galvanized steel wire according to the world market price for steel wire to Southwire, a Georgia company. *Id.* at 1065. Disputes arose over the interpretation of the world market price, alleged corrosion of the goods, and alleged flaking of the zinc coating on the wire. *Id.* Laminoirs submitted the disputes to arbitration in accordance with the arbitration clause, the arbitration clause contained a

public policy was identified by referring to a violation of substantive law. However, it gives a clear reference to the lack of consensus on the principles of international public policy, where it attempted to use transnational public policy by relying on its principles. However, in the absence of a consensus, such principles regarding interest cannot be applied, and so far there is no uniform international rules in this regard. Therefore, the concept of transnational public policy also cannot be applied in this respect.

6.2.1.2 Applying the concept of international public policy

Although there are a few countries applying the term 'international public policy' with regard to the rules of international justice, such countries attempted to make this concept narrower than the concept of national public policy in some aspects.⁹⁴⁹ Such interpretations are debatable and they have not yet an clearly to appropriate meaning. A report of the Commission of the United Nations stated that 'It was understood that the term 'public policy', which was used in the NYC and many other treaties, covered fundamental principles of law and justice in substantive and procedural respects'.⁹⁵⁰ The international concept would lead to increased conflicts between laws and systems even with regard to a single issue. Thus, it is very difficult to unify opinion on the definition of international public policy when there are various rules of justice in relation to interests. French theory does not apply the practice in general because it does not distinguish between procedural or substantive rules. Thus, when we distinguish between those rules, we do not need the concept of international public policy, so each state has its sovereignty, taking into account the freedom of the parties and the nature of arbitration.

governing law clause that Georgia law, to the extent that it is in accordance with French law, would govern the arbitration. *Id.* at 1065. and the arbitration panel held that Southwire owed Laminoirs for the higher world market price plus interest at the French legal interest rate. *Id.* 1065. When Laminoirs attempted to enforce the award, Southwire argued that the French interest rate violated the enforcing forum's public policy because it was usurious. *Id.* Although the French interest rate was higher than that of Georgia, where the French interest rate ranged from 9.5% to 10.5% per year. *Laminoirs*, 484 F. Supp. at 1069. The Georgia interest rate was 7% per year, but rates of interest as high as that of the French were not prohibited by Georgia law. *Id.* However, court concluded that it was not so high as to constitute a violation of the "forum country's most basic notions of morality and justice." *Id.* at 1068-69 (citing *Parsons & Whittemore Overseas Co. v. Societe Generale de L'Industrie du Papier (RAKTA)*, 508 F.2d 969, 974 (2d Cir. 1974)). Thus, the application of the French interest rate was not contrary to public policy. *Id.* at 1069. However, the court went further and analysed the additional increase of 5% interest per year. *Id.* The court noted that the purpose of interest is to make whole a person who is deprived of the use of his money rather than to penalize the wrongdoer. *Id.* According to Georgia public policy, "[a] foreign law will not be enforced if it is penal only and relates to the punishing of public wrongs as contradistinguished from the redressing of private injuries." *Id.* (citing two Georgia cases). Thus, the additional 5% interest was contrary to public policy because it was not reasonably related to the damage Laminoirs suffered due to the delay in receiving the awarded sums. *Laminoirs*, 484 F. Supp. at 1069. While the court enforced the award so far as the application of the French interest rate, it refused to enforce the additional 5% interest. *Id.* Thus, the U.S. court accepted the public-policy defence with some limitations.

⁹⁴⁹ Henriques and Advogados 'The very circumstance that the rules in question are deemed to be absolutely mandatory would also have the 'general characteristic' of the international public policy.'

⁹⁵⁰ United Nations Document A/40/17, Section 297, the instances such as corruption, bribery and fraud and similar serious cases would constitute a ground for setting aside [the award]. It was noted, in that connection, that the wording 'the award is in conflict with the public policy of the State' was not to be interpreted as excluding instances or events in relation to the manner in which it was arrived at'.

It does not follow that if the dispute contains a foreign element it is bound to be within the international public policy, which is 'international' in the sense that it operates in the field of private international law as applies to transactions involving foreign elements. Private international law is part of a nation's national law and therefore differs from nation to nation. Although, public international law is primarily concerned with dealings between sovereign nations, it is becoming increasingly applicable to commercial transactions involving private parties.⁹⁵¹ However, that should not cause confusion between private and public international law. International public policy can nevertheless extend to the protection of interests that are common to the international community at large.⁹⁵² International public policy may not protect the interests of the state itself unless laws on interests were consolidated. Issues that are related to the dispute in arbitration are in the scope of private international law and it is not possible to apply such concepts where they cannot be applied to peremptory norms and rules of international justice.

6.2.2 *Transnational public policy*

Transnational public policy is a world-wide public policy that has a controlling function toward the laws of all states globally.⁹⁵³ The transnational public policy is the policy that combines several countries, and often reflects common interests shared between these countries. Examples include the public policy of the European Union countries⁹⁵⁴ and that of Islamic countries.⁹⁵⁵

Transnational public policy was established with the concept of natural law in the classical era, and natural law was seen then as a set of unwritten norms with a higher standing than the imperfect statutes of the *polis*.⁹⁵⁶ Although the concept of transnational public policy includes the basic rules of natural law and principles of international justice, it still not agreed upon everywhere.⁹⁵⁷ The concept is unable to determine these rules or principles as there are no adequate cases to support the notion of transnational public policy. The principle of transnational public policy has both negative and positive functions within a set of rules. In its negative function

⁹⁵¹ Lew, Mistelis and Kröll 18.71–18.73., note the application of public international law by several ICC and *ad hoc* commercial arbitrators. The WTO has also developed public international law, which is relevant to commercial transactions.

⁹⁵² AN Zhilsov, 'Mandatory and Public Policy Rules in International Commercial Arbitration' (1995) 42 *Netherlands International Law Review* 81, 99–100.

⁹⁵³ Lew, Mistelis and Kröll 475–503.

⁹⁵⁴ *Eco Swiss China Time Ltd v Benetton International NV* [2000] 5 CMLR 816.

⁹⁵⁵ Redfern 2–67; Mistelis 251.

⁹⁵⁶ See Raoul C Van Caenegem, *An Historical Introduction to Private Law* (Cambridge University Press 1992) 117; Martha Craven Nussbaum, *The Fragility of Goodness: Luck and Ethics in Greek Tragedy and Philosophy*, vol 2 (Cambridge Univ Press 2001); Thomas G West and Platon, *Plato's Apology of Socrates: An Interpretation, with a New Translation* (Cambridge Univ Press 1979); Leo Strauss, 'On Plato's Apology of Socrates and Crito' (1976) 1983 *Essays on Honor of Jacob Klein*, St. John's College Press, reprinted in Leo Strauss 38.

⁹⁵⁷ ILA Report 259. For instance, in *Fougerolle v Procofrance* (1990) Rev. Arb. 892, the Paris Court of Appeal in France expressed a degree of scepticism in relation to applying transnational public policy.

it is used as a shield⁹⁵⁸ to protect against any attack to the international community.⁹⁵⁹ Mantilla-Serrano addresses the issue of fundamental procedural rules in transnational public policy in his research and gave some thoughts in this regard. He shows that the term “transnational” goes beyond nations, which is different from the term international, which means between States. The author mentions that where there is no specific definition of the term transnational, the meaning in this context means consensus regarding the procedural public policy. The existence of these rules is based on the need of most legal systems to support these basic procedural rules. Mantilla-Serrano also believes that the procedural rules in transnational public policy get their sources from the procedural rules of arbitration of international organisations, international arbitration laws of the States, the seat of the arbitration, and the NYC 1958.⁹⁶⁰ Hunter and Silva argue that transnational public policy is more consistent and narrower in scope than the international public policy of the state.⁹⁶¹ The concept of transnational public policy may have a narrower scope in general than the public policy of the country in which the arbitral award will be enforced, but may give a wider scope to that country regarding the merit of dispute. It noted the intervention of concepts with respect to the international public policy, transnational public policy and national public policy, and the possibility of the application of mandatory rules or basic principles. However, the concept of the transnational public policy is similar to the international public policy in general.

Many authors believe that the differentiation between transnational public policy and international public policy of the State comes from the approach of private international law⁹⁶². Most the controversy in arbitration is in the settlement of disputes and the substantive provisions of international conventions, not on the legal relationship between contracting parties, which is between the investor and the host country.⁹⁶³ Indeed, the controversy is in the substantive issues of the conflict, the mandatory rules, and substantive rules of chosen law that are related to the place of enforcement under public policy. They believe that the sources of transnational public policy include the basic principles of the natural law, international justice, peremptory norms and

⁹⁵⁸ Lew, Mistelis and Kröll 475–503. See also Pierre Lalive, ‘Transnational (or Truly International) Public Policy and International Arbitration’ in Pieter Sanders (ed), *Comparative Arbitration Practice and Public Policy in Arbitration* (Kluwer Law International 1987) 289.

⁹⁵⁹ See P Lagarde, ‘Public Policy, International Encyclopedia of Comparative Law, Vol III’ [1994] Mohr, Tübingen 9. The international community includes states, corporations, individuals and international organizations.

⁹⁶⁰ Fernando Mantilla-Serrano, ‘Towards a Transnational Procedural Public Policy’ (2004) 20 *Arbitration International* 333, 337.

⁹⁶¹ Martin Hunter and Gui Conde e Silva, ‘Transnational Public Policy and Its Application in Investment Arbitrations’ (2003) 4 *The Journal of World Investment* 367, 367 <http://www.arbitration-icca.org/media/0_12232929401680/martin_and_gui_conde_e_silva.pdf>.

⁹⁶² Martin Hunter and Gui Conde e Silva, ‘Transnational Public Policy and Its Application in Investment Arbitrations’ (2003) 4 *The Journal of World Investment* 367, 367.

⁹⁶³ But not all. See, e.g., ICC arbitration *SPP v Egypt*, Yearbook Commercial Arbitration, vol. XIX, 1994, 51 et seq; Martin Hunter and Gui Conde e Silva, ‘Transnational Public Policy and Its Application in Investment Arbitrations’ (2003) 4 *The Journal of World Investment* 367, 367

general principles of morality accepted by civilised nations.⁹⁶⁴ However, again it reflects the concept of international public policy, where it is clear that there is a similarity with the principles of transnational public policy. There are also those who believe that there are a large number of rules involved and these rules identify the transnational law, making it necessary to distinguish public and private international norms⁹⁶⁵ that may be applied in case of a conflict of rules.⁹⁶⁶

6.2.2.1 The problems of applying transnational public policy

Although Lalive argues that transnational public policy and national public policy do not differ in their application when the public policy of the state may maintain the fundamental interests of the state itself, transnational public policy may maintain the vital interests of the international community.⁹⁶⁷ Unfortunately, this perception is not entirely true, as national public policy takes into account national interests that are compatible with its society and legal system, unlike transnational public policy which may be incompatible. Transnational public policy is contrary to the public policy of the state and its law when it is not part of national public policy and there is no unified international laws or uniform rules with regard to commercial disputes, specifically usury and compensation.⁹⁶⁸ It means this approach cannot be used and thereby the concept of transnational public policy is not appropriate for all situations of conflict. Mantilla-Serrano argues that the NYC, the Model Law, the domestic arbitration rules of states, and judicial rulings all agree to give the parties the opportunity and the freedom to submit their disputes and become part of the transnational public policy.⁹⁶⁹ The application of national policy does not mean ignoring the interests of the international community where such public policy includes international conventions. Most countries take into account the interests of other signatory countries, but these considerations must not exceed the national interests or national laws. Saudi Arabia, for example, takes into account reciprocity and international and regional conventions.

The freedom of the parties may be considered a substantive mandatory rule since all the laws and organisations refer to this rule. It is applicable in accordance with international conventions and domestic laws but not through the application of the concept of transnational public policy. Moreover, there is interference between private and public international law which causes an inability to distinguish between international or transnational public policy. Further complications are caused by differences in the sources of public and private international law. In

⁹⁶⁴ Hunter and Conde e Silva.

⁹⁶⁵ Emmanuel Gaillard, 'Transnational Law: A Legal System or a Method of Decision Making?' (2001) 17 *Arbitration International* 59, 59–72.

⁹⁶⁶ Jean-Baptiste Racine, *L'arbitrage Commercial International et L'ordre Public*, vol 309 (LGDJ 1999) para 763.

⁹⁶⁷ Lalive, 'Transnational (or Truly International) Public Policy and International Arbitration' 313.

⁹⁶⁸ As is the case in apartheid, drug trafficking and corruption ...etc. where is contrary to public policy of most of the countries in the international community, which is considered sufficient justification for refusal of enforcement. See Savage and Gaillard.

⁹⁶⁹ Mantilla-Serrano.

the case of arbitration, it is not based only on the conventions and is not part of public international law, but rather in the domain of private international law. Hence, it must respect the laws relating to aspects of the conflict. It can rely on the rules applicable in international contracts and mandatory rules governing international trade, which is a process of internationalisation of the law.⁹⁷⁰ However, in the absence of this understanding and agreement, it is still within the scope of private international law and therefore within national law, which is part of private international law.⁹⁷¹ Internationalisation of private law and the development of customary international law '*lex mercatoria*' has not so far sufficiently addressed the issue of usury. Usury may be considered as forbidden internationally except in some countries under different rates, and it is contrary to the rules of justice and public policies in others.

In short, arbitration in public international law cannot expressly defined with regard to interest laws and arbitration so far is within the scope of private international law. International public policy in private international law cannot be achieved because these principles are not limited to this concept and there is no unity of views. To implement this concept, public policy should first consider disputes concerning usury or interest and unify the procedural and substantive rules at least on a regional scale. Terminology such as 'international' does not necessarily refer to the international or the transnational public policy, and arbitration takes place in different countries under international arbitration agreements. Unless such laws become unified, including usury laws, it cannot become Islamist or transnational public policy. Thus, any breach of the provisions or the choice of the law of contract will be considered a breach of international or transnational public policy according to these principles.

6.2.3 *National public policy*

Art V (2) of the NYC gives countries the opportunity to reject the recognition and enforcement of non-arbitrable matters if contrary to the public policy of the place of enforcement. Art V (2)(a) refers expressly to the law of the place of enforcement, which means such law is considered. In contrast, Art V (2) (b) refers explicitly to the public policy of the place of enforcement; it does not indicate any of the other concepts. The concept of public policy is unclear and remains ambiguous.⁹⁷² All categories of public policy are shared; basic principles of justice and morality shape the fundamental interests of political, social and economic interest, mandatory rules and obligations toward other countries. The concept of national public policy based so on many rules is able to protect these interests, where a state can maintain its own interests through

⁹⁷⁰ JD Fry, 'Desordre Public International under the New York Convention: Wither Truly International Public Policy' (2009) 8 Chinese Journal of International Law 81, 92 <<http://chinesejil.oxfordjournals.org/cgi/content/long/8/1/81>> accessed 30 April 2014.

⁹⁷¹ JG Collier and JG Collier, *Conflict of Laws* (Cambridge University Press 2001) 390.

⁹⁷² *DST v Rakoil BT - Lloyd's Rep 2* (1987) 1987 246 Sir John Donaldson stated; 'consideration of public policy can never be exhaustively defined, but they should be approached with extreme caution'.

the enactment of special laws. In contrast, international conventions serve and protect the interests of the international community and there is no need to use other concepts to serve these interests.

6.2.3.1 Examples of applications of national public policy

Many countries follow this approach, such as Germany, Austria, Sweden, Poland, Brazil, and China as well as some Islamic states including Saudi Arabia, Egypt, UAE and Kuwait. In addition, the U.S. has different approaches in different states, while in England the approach is not clear. Some argue that England adopts international public policy,⁹⁷³ but in some cases it clearly adopted national public policy.⁹⁷⁴ However, most of these countries strongly believe that a violation of the law constitutes a violation of public policy, with some ambiguity in some aspects.

6.2.3.2 Problems of national public policy

The ambiguity of international and transnational public policy makes countries resort to national law and the rule of law in many cases. Cairns observes that states rely on their internal laws to escape the enforcement of foreign arbitral awards.⁹⁷⁵ According to Lew, public policy reflects the fundamental economic, legal, moral, political, religious and social standards of each State or national community.⁹⁷⁶ The rule of law includes substantive and procedural rules;⁹⁷⁷ all the rules of law have a direct impact and are part of the public policy.⁹⁷⁸ Such procedural and substantive rules are part of the law of the seat of arbitration, the law governing the contract, and the law of the country of enforcement where the national law is considered a part of the arbitration process. The national procedure law is part of private international law; thereby the abolition of internal law is the abolition of public policy in some aspects. Therefore, national law can be said to be considered the biggest influence in international arbitration.

Recognition and enforcement of foreign arbitral awards may be refused in the event of a conflict with procedural and substantive rules. These countries often refer to the substantive rules in an attempt to protect these rules, due to the lack of a uniform definition of public policy and

⁹⁷³ See e.g. Johannes Berning Robertson, 'Public Policy as a Ground for the Refusal to Enforce International Commercial Arbitration Awards' 7 <<http://dspace.nwu.ac.za/handle/10394/8422>>; *Ispahani v Bank Melli Iran BT - Lloyd's Rep Bank* (1998) 1998 133 (English Ct. App.) [133] 'for English courts to consider foreign public policy, carrying out of prohibited acts within foreign country is an essential element'.

⁹⁷⁴ See e.g. *Dallah Real Estate BT - UKSC* (2010) 2010 46; See also *Vervaeke v Smith BT - AC 1* (1983) 1983 145 [146] stated that contrary justice or morality and interest of United Kingdom is violation public policy.

⁹⁷⁵ David Cairns, 'Transnational Public Policy And The Internal Law Of State Parties' (2009) 6 *Transnational Dispute Management* <<http://www.cremades.com/pics/contenido/File634523788247688756.pdf>>.

⁹⁷⁶ Julian DM Lew, 'Applicable Law in International Commercial Arbitration. A Study in Commercial Arbitration Awards' (1978) 1 Dobbs Ferry, NY: Oceana Publications and Leiden: Sijthoff & Noordhoff, 1978 532.

⁹⁷⁷ 'ISLAMIC LAW & INTERNATIONAL LAW' (INTERNATIONAL LAW ASSOCIATION 2012) 3 <<http://www.ila-hq.org/en/committees/index.cfm/cid/1006>>.

⁹⁷⁸ Christoph Liebscher, 'European Public Policy' (2000) 17 *Journal of International Arbitration* 73, 76.

ambiguity in this concept. It seems that there is a relationship between public policy and national law, and between mandatory, substantive and procedural rules, and there is an inverse relationship between public policy and substantive rules, which means that the public policy may include substantive rules and the substantive rules may include public policy.

6.2.3.3 Problems in national public policy in usury and interest

National public policy is still used incorrectly and with different interpretations, although there is a convergence between national public policy and the national law. It is not limited to the subject of international arbitration, but extends to domestic arbitration. Confusion lies in the interpretation of such concepts by the national courts and in applications of public policy by the courts. Neither is it limited to a certain country; this confusion exists in most countries.

Public policy is indistinguishable in all Islamic countries. Egypt and UAE have allowed interest-based loans and debts, which may create conflicts between such countries. Part of Saudi public policy is contrary to *Sharia* itself, but would not be contrary to public policy in Egypt or the UAE regarding bank practices. Legally, the Egyptian law regarding interest-based loans is contrary to *Sharia* law and thus unenforceable in Saudi Arabia. In addition, the concepts of public policy in some of these countries conflict with each other. The UAE is more complex and is unsteady on the concept of public policy, *Sharia* law and its domestic law in practice and in the definition of usury. It is worthy of note that the judicial provisions and public policy in Egypt would give effect to the enforcement request.⁹⁷⁹ However, if the arbitral award is subject to a foreign law, it would not constitute a violation of public policy in Egypt.⁹⁸⁰

Thus, there is a spiral of conflicts in these countries: starting with conflicts between their constitutions and the law, their public policy and the law, and finally conflicts between their law and *Sharia* law under such convention (see Chapter Four). Islamic countries apply *Sharia* and Civil Law together but vary in the level of *Sharia* as a source of national law. The confusion is evident in Saudi Arabia and UAE. Thus, practically, all these countries allow usurious transactions in banks and others practice, although they are prohibited under *Sharia* law.

In Dubai, the Court of Cassation 'ruled that not all imperative (mandatory) rules are part of public order'.⁹⁸¹ Thus, 'the rules of evidence, for instance, are mandatory rules but form no part

⁹⁷⁹ Act (58) (2) of the Egyptian Arbitration Law 1994 "The application to obtain leave for enforcement of the arbitral award according to this Law shall not be granted except after having ascertained the following:

a) That it does not contradict a judgment previously rendered by the Egyptian Courts on the subject matter in dispute;
b) That it does not violate the public policy in the Arab Republic of Egypt."

⁹⁸⁰ See ICC arbitral award CK/9928 rendered on December 21 1999.

⁹⁸¹ See Federal Supreme Court, petition no 209 for the year 15, dated 22 January 1995 and the Dubai Court of Cassation, petition no 146/2008, judgment dated 9 November 2008. cited in Habib Al Mulla, 'Arbitration under UAE Law: Towards a Modern Legal Framework?' (*In House Lawyer*, 2010)

<<http://www.inhouselawyer.co.uk/index.php/united-arab-emirates/8140-arbitration-under-uae-law-towards-a-modern-legal-framework>> accessed 16 October 2015.

of public order'.⁹⁸² However, the courts refer only to narrow national public policy and not to any international public policy.⁹⁸³ In contrast, Art 216 of the Civil Procedure Code refers to public policy as one of the reasons for refusal of enforcement; the court may focus only on issues that may contain elements of usury. It was noted that usury violates public policy and its basic principles.⁹⁸⁴ This means that contracts which contain elements of usury are against the public policy of UAE and one of the mandatory rules of the State.⁹⁸⁵

The Abu-Dhabi Court of Appeal ruled in *A.A Commercial Co. v. S. Motors Ltd Co. and D. Industrial Ltd Co.*⁹⁸⁶ that applying a foreign law or arbitration that takes place outside the country under foreign law is not contrary *Sharia* merely because it is foreign, unless it violates *Sharia*. In *G. Steel Industry Co. v. International Steel and Contractors Co.*,⁹⁸⁷ the Federal Supreme Court held that the arbitration agreement outside the country does not violate *Sharia* if the arbitral award is within the scope of *Sharia*. However, in Dubai, the court ignored the provisions of the NYC and the bilateral agreement between the UAE and France, and refused to enforce three awards.⁹⁸⁸ In a similar case in Dubai, the court enforced an award in a situation similar to the issue above, and the Court said that there was no conflict with public policy.⁹⁸⁹

However, the actions were contradictory due to the power of the judicial authority in those cases. In the second case, the judicial supervision of the Court of Appeal was limited to verification of the absence any a violation of Federal Decree No. 43 of 2006. The court must ensure that the award fulfils the formal and substantive elements required where the concept of public policy includes substantive rules.⁹⁹⁰ In contrast with the first case, the enforcement of the arbitral award was rejected by the national court.⁹⁹¹ This is a clear example of the confusion in the concept of public policy and there may be a relationship between the authority of the courts, public policy and its interpretations.

⁹⁸² See Habib Al Mulla, 'Arbitration under UAE Law: Towards a Modern Legal Framework?' (*In House Lawyer*, 2010).

⁹⁸³ Habib Al Mulla, 'Arbitration under UAE Law: Towards a Modern Legal Framework?' (*In House Lawyer*, 2010).

⁹⁸⁴ Court of Cassation – Dubai – challenge no 146 of 2008 civil- November 9, 2008.

⁹⁸⁵ See e.g. Kanakri 217–225.'

⁹⁸⁶ Case No 10007/1981.

⁹⁸⁷ UAE Supreme Court Case No 138/10.

⁹⁸⁸ Case No. 489/2012, see Gordon Blanke and Habib Al-Mulla, 'Recent Ruling of Dubai Court of Cassation on Enforcement of Foreign Arbitral Awards: Back to Square One It Is ...' (*Kluwer Arbitration Blog*, 2013) <<http://kluwerarbitrationblog.com/blog/2013/10/21/recent-ruling-of-dubai-court-of-cassation-on-enforcement-of-foreign-arbitral-awards-back-to-square-one-it-is/>> accessed 16 October 2015.

⁹⁸⁹ Case No. 1/2013, considered by the Court of Appeal cited in Gordon Blanke and Habib Al-Mulla, 'Recent Ruling of Dubai Court of Cassation on Enforcement of Foreign Arbitral Awards: Back to Square One It Is ...' (*Kluwer Arbitration Blog*, 2013).

⁹⁹⁰ Blanke and Al-Mulla, 'Recent Ruling of Dubai Court of Cassation on Enforcement of Foreign Arbitral Awards: Back to Square One It Is ...'

⁹⁹¹ Gordon Blanke and Habib Al-Mulla, 'Recent Ruling of Dubai Court of First Instance on Enforcement of Foreign Arbitral Awards: Back to Square One?' (*Kluwer Arbitration Blog*, 2013) <<http://kluwerarbitrationblog.com/blog/2013/03/12/recent-ruling-of-dubai-court-of-first-instance-on-enforcement-of-foreign-arbitral-awards-back-to-square-one/>> accessed 16 October 2015.

As we have seen, practice in the UAE in commercial law allows simple interest, and in some cases compound interest, which are both considered usury under *Sharia*. On the other hand, usury is non-arbitrable in UAE and is against public policy (see Chapters Four and Five). It seems that higher interest rates are illegal, and therefore usury is non-enforceable due to the non-arbitrable and public policy exceptions. Thus, there is a misunderstanding regarding the mandatory rules and public policy and their applications in the UAE due to the lack of a statement from the legislature as well as the national courts, and the contradictions in their interpretations of those rules.

Some countries in the Middle East continue to review arbitral awards and their merits to make sure that these awards do not conflict with public policy or *Sharia* law.⁹⁹² This means that there are still problems with the enforcement of foreign arbitral awards and their relationship to public policy. The problem lies in the interpretation of exceptions to the NYC, and specifically the issue of public policy in the convention and in those laws. There are three areas of concern:

- 1 - usury laws;
- 2 - usury under *Sharia* law; and
- 3 - usury under public policy.

These countries, including Saudi Arabia, have been criticised as ‘having the cake and eat[ing] it’,⁹⁹³ which has led to a loss of confidence in the NYC when arbitration involves a country which allows review of foreign arbitral awards.⁹⁹⁴ Critics condemned the NYC, which allowed Saudi Arabia to benefit from the methods of settlement of international disputes, while in contrast it retains the option to refuse to enforce foreign arbitral awards that are inconsistent with public policy.⁹⁹⁵ Roy described⁹⁹⁶ Saudi Arabia as ‘traditionally hostile to the recognition and enforcement of non-domestic arbitral awards’. All of this prejudice against Saudi Arabia is because of a lack of clarity of the concept of public policy and *Sharia* law. The fact is that this ambiguity in the concept of public policy is not limited to Saudi Arabia, which is seen using the

⁹⁹² Gemmell (n 114)169; Kristin T Roy, ‘The New York Convention and Saudi Arabia: Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards?’ (1994) 18 Fordham International Law Journal 953–54.

⁹⁹³ See Charles N Brower and Jeremy K Sharpe, ‘International Arbitration and the Islamic World: The Third Phase’ [2003] American Journal of International Law 643, 656; See also Kristin T Roy, ‘The New York Convention and Saudi Arabia: Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards?’ (1994) 18 Fordham International Law Journal 951.

⁹⁹⁴ Kristin T Roy, ‘The New York Convention and Saudi Arabia: Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards?’ (1994) 18 Fordham International Law Journal 954.

⁹⁹⁵ Samir Saleh, *Commercial Arbitration in the Arab Middle East: A Study in Sharia and Statute Law* (1st edn, Graham & Trotman 1984) 225; .

⁹⁹⁶ Kristin T Roy, ‘The New York Convention and Saudi Arabia. Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards?’ (1994) 18 Fordham International Law Journal 953.

concept of public policy to defend the public interests according to its political interests.⁹⁹⁷ The concept of public policy has been misinterpreted and misapplied in these countries. In fact, there are those who demand a narrowing of the concept of public policy,⁹⁹⁸ or that it be dispensed with altogether.⁹⁹⁹ This is not limited to Saudi Arabia, but Saudi may be the most complex example, because of the codification of *Sharia* law in relation to commercial transactions.

In Saudi Arabia, the matter of usury is very sensitive and non-negotiable, and there is often misunderstanding between the international community and the Saudi regime on this issue. Although there is a striking similarity between Saudi law and UNCITRAL,¹⁰⁰⁰ there is a difference where Saudi arbitration law requires that arbitral awards should not be contrary to both *Sharia* law and public policy in Saudi Arabia. Thus, Saudi Arabia reviews and rejects foreign arbitral awards that do not meet this test;¹⁰⁰¹ it is having the cake and eating it, whether public policy in Saudi Arabia is in line with *Sharia* law or not. Saudi Arabia, as a member of the NYC, can take advantage of the Convention with regards to exceptions to recognition and enforcement of the foreign arbitral award like other members, but Saudi Arabia refuses to enforce foreign arbitral awards which contain any element of *Riba* because the existence of such an element is contrary to public policy.¹⁰⁰² Public policy in Saudi Arabia remains unclear, as do the standards that are applied during the enforcement process.¹⁰⁰³ This ambiguity has caused in the creation of more conflicts around the concept of public policy and its interpretations.

Previously, in some cases, public policy has been defined widely by the courts and enforcing a foreign law would be contrary to Saudi public policy.¹⁰⁰⁴ Public policy may be in conflict with *Sharia* law. The enforcement of the award faces two fundamental requirements in the Saudi law, which means it is all but impossible to be enforce a foreign arbitral award in such circumstances. To settle these disputes, a radical solution should be found, and not just exceptions by the courts, where it is possible that judges would make it more difficult due to their varying interpretations. By clarifying public policy, the confusion and conflict would be removed. The function of arbitration is to settle disputes, not to create them.

⁹⁹⁷ Born 3340.

⁹⁹⁸ Professor Pierre Mayer (France): Chairman Mr Audley Sheppard (UK): Co-Rapporteur Dr Nagla Nassar (Egypt): Co-Rapporteur, 'ILA Report, International Law Association Committee on International Commercial Arbitration' (2000).

⁹⁹⁹ Kristin T Roy, 'The New York Convention and Saudi Arabia: Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards?' (1994) 18 Fordham International Law Journal 922-57.

¹⁰⁰⁰ Born 3340.

¹⁰⁰¹ Saudi Arbitration Law Articles 5 and 50 (2).

¹⁰⁰² Baamir (Ashgate 2010) 180; Gemmell (n 114)189; Kutty (n 25) 602.

¹⁰⁰³ See Ahdab AH and El-El-Ahdab 612-13; Kutty (n 25) 602-603; Michael J.T. McMillen, *Islamic Sharia-Complaint Project Finance: Collateral Security and Financing Structure Case Studies*, 24 FORDHAM INT'L L.J. 1184, 1201-02 (2001).

¹⁰⁰⁴ Ahdab AH and El-El-Ahdab J, *Arbitration with the Arab Countries* (Kluwer Law International 2011)

6.3 The relation between the law and public policy

Positive law and public policy both are variable in their elements, but the public policy may follow the law, and *vice versa*. In the traditional approach, the constitution is created by votes and specialised committees in accordance with the rules of general morality and justice under public policy. There is a symbiotic relationship between law and public policy; the law defines public policy, and public policy defines the law. In Civil Law, most countries refer to an international public policy wider than written codes, but some refer to such codes as public policy, like Germany. Common law countries such as the U.S. refer mostly to case law, especially for substantive law. Islamic countries do not often have a clear definition of public policy, creating more confusion in arbitration when compared to the U.S., where courts intervene in the validity of arbitration agreement. Thus, in many cases the arbitral award would be rejected under the law and public policies in different states under different approaches. Issues include waivers of non-waivable statutory rights,¹⁰⁰⁵ punitive damages,¹⁰⁰⁶ charging interest above the legal limit,¹⁰⁰⁷ or actual damages. This causes significant problems in inter-state trade, where an agreement enforceable in California may not be enforceable in Texas (see Chapter Five).¹⁰⁰⁸

Public policy in the U.S. is broad¹⁰⁰⁹ and not defined through legislation, constitutional norms or judicial decisions, but judicial decisions are considered reliable source of public policy.¹⁰¹⁰ It has been recognized by U.S. federal and state courts that there is a narrow exception to the application of mandatory interest laws which use the rate set by the parties rather than the legal rate if the parties have agreed upon, and expressly provided for, the interest rate.¹⁰¹¹ Therefore, this narrowly-defined exception allows absolute freedom of the parties in spite of the absence of the concept of international public policy. The enforcing court may refuse to implement the part of an award that includes interest on the basis of its punitive nature, usury or public policy,¹⁰¹² however, principles of justice regarding interest vary between different states and that causes conflicts even within a single country. Consequently, compared with the Saudi

¹⁰⁰⁵ *Buckeye Check Cashing, Inc v Cardegna BT - US* (2006) 546 440; *Bridge Fund Capital Corp v Fastbucks Franchise BT - F 3d* (2010) 622 996 [999, 1003 and 1005].

¹⁰⁰⁶ *Bridge Fund Capital Corp v Fastbucks Franchise BT - F 3d* (2010) 622 996 [999 and 1003]; D Laycock, *Modern American Remedies: Cases and Materials* (Aspen Law & Business 2002) 732–736.

¹⁰⁰⁷ *Pang v INTERNATIONAL DOCUMENT SERVICES BT - UT* (2015) 2015 63 [5–6]; *Williams v CashCALL, INC*; See e.g. *Nagrampa v MailCoups, Inc BT - F 3d* (2006) 469 1257 [1269]; *Armstrong v Steppes Apartments, Ltd BT - SW 3d* (2001) 57 37. *Bridge Fund Capital Corp. v. Fastbucks Franchise BT - F. 3d* [999 and 1003].

¹⁰⁰⁸ *Buckeye Check Cashing, Inc. v. Cardegna BT - US; Nagrampa v. MailCoups, Inc. BT - F. 3d, Williams v. Cash CALL, INC.*

¹⁰⁰⁹ *Pang v. INTERNATIONAL DOCUMENT SERVICES*, 2015 U.T. 63 (Utah 2015). [24–27].

¹⁰¹⁰ *Pang v. INTERNATIONAL DOCUMENT SERVICES*, 2015 U.T. 63 (Utah 2015). 14–24.

¹⁰¹¹ *Westinghouse Credit Corp v D'URSO BT - F 3d* (2004) 371 96 [101–102] 'We agree that parties may by contract set a post-judgment rate at which interest shall be payable...It is well-established that parties can agree to an interest rate other than the standard one contained ... provides a standard rate of post-judgment interest, the parties are free to stipulate a different rate, consistent with state usury and other applicable laws'.

¹⁰¹² Redfern, Hunter and Partasides .

practice, the level of confusion is much lower among these interpretations. Although there is still confusion about the conflict of public policies in different states, judicial decisions are a reliable source of public policy. All judicial decisions refer to the specific law in each state as public policy and violating such laws is contrary to public policy. In England the concept is unclear as both law and public policy depend on the interpretation of the judge. This is because breaches of public policy may be found on the basis of public policy itself, or a breach of procedural provisions.

As stated, the concept of public policy consists of different principles in different jurisdictions. It consists of mandatory rules, the rules of national justice, public morality, and national interests. The purpose of public policy is to protect the fundamental principles of society, which differ from one society to another. National law takes into account the identification and protection of these principles, regulates national and international transactions, and determines the rules of morality and justice. The central point of the rejection of foreign arbitral awards is a violation of national law, where there is a close relationship between law and public policy.

6.3.1 *Public policy under Sharia law*

Similarly, public policy in *Sharia* law can be determined by the rules of *Sharia* law and its sources.¹⁰¹³ However, with regard to the regulations in Islamic countries, which consider *Sharia* a primary source, these regulations are subject to the concept of *Siyasah Shar'iyah* (legitimacy policy).¹⁰¹⁴ This concept allows enacting laws that do not exist within the sources of *Sharia* law, but should not conflict with *Sharia* itself or its rules. Thus, *Sharia* has one integrated system which determines public policy by defining principles of transactions, economic and social interest and public morals. In Saudi Arabia, *Sharia* law determines public policy, which includes Royal Decrees and regulations, which do not conflict with the sources of *Sharia* law. The Implementing Regulations of the old arbitration law expressly stipulated that public policy is *Sharia* law. Art 11 of the Enforcement Law of 2013 and its executive regulations state clearly that public policy is *Sharia* law.

The term “public policy” has been repeated in most internal laws equally to the term “*Sharia* law” term where public policy, public order or public system all follow *Sharia* principles. Because the concepts are not clearly defined in separate terms, this creates confusion in legal processes. Debates on the real meaning of such repetitions arose due to the impossible definition of the concept of public policy dealing with *Riba* as a result of the disagreement within the practice (SAMA) of the committees and of the Saudi court system. It is because of court provisions and

¹⁰¹³ 'ISLAMIC LAW & INTERNATIONAL LAW' 8; Ali Ahdab and Jalal El-Ei-Ahdab, *Arbitration with the Arab Countries* (Kluwer Law International 2011) para 261; Kutty (n 25) 610-611.

¹⁰¹⁴ Mohammad Hashim Kamali, 'Beyond the Shari'ah: Siyasah Shar'iyah and Its Application' (2005) 10 *Al-Shajarah: Journal of the International Institute of Islamic Thought and Civilization (ISTAC)*.

Sharia law being the main source of the Saudi law that the confusion was made. It should be more appropriate to retain *Sharia* law temporarily, and perhaps the reason for all the contradictions is due to a lack of knowledge of the *Sharia* procedural and substantive rules with regard to *Riba*.

Regardless of erroneous practices, the prohibition against *Riba* is considered a substantive matter under *Sharia* law, thus a dispute that includes such a matter constitutes violation of substantive public policy and substantive *Sharia* law in Saudi Arabia. In contrast, the rest of the compensation cases, with the exception of compensation for delayed payment, are considered procedural issues. The contradiction is that in *Sharia* law, the mandatory law is only the substantive law. Thus, erroneous practices failed to guide practitioners to an absolute definition of public policy, especially in Saudi Arabia. For instance, the confusion can be found in Art 55 of the Saudi Arbitration Law, where the enforcement of an arbitral award would be rejected if it is contrary to *Sharia*, public policy, or a previous judgment issued by a competent authority. The provisions of the committees may be considered contrary to the provisions of Saudi justice and therefore an award that is issued with respect to payment of interest may be in conflict with either the rulings of the Saudi courts or legal committees under SAMA. The Saudi courts adhere to the consideration of the cases in accordance with *Sharia* law. There is also a legal error in the article, which does not take into account the practices of legal committees with regard to *Riba* (see Chapter Three).

Thus, there is a challenge in defining the concept of public policy in Islamic countries that combine the traditional approach and *Sharia* law, which leads to more conflicts. Obviously, public policy in such countries is determined according to the adoption and power of *Sharia* sources, whether considered as a primary source or one of the sources of law, but public policy in such countries is a mixture between the traditional approach and *Sharia* law. Therefore, public policy in these countries cannot be considered as grounds for rejection, but rather refers to the law itself. The issue of usury is a thorny one which would cause rejection of many awards in many countries under public policy. However, when applying the concept of domestic public policy, it becomes easier for the existence of the relationship between law, ‘which determines the rules of justice and morality’, and public policy. Thus, relying on the law does not conflict with public policy and the misinterpretation public policy may be contrary to public policy itself.

6.3.2 *The determination of public policy*

In addition to confusion over the applicable law to the merit of dispute or the arbitral agreement, there is also confusion as to who observes whether the arbitrators should consider the public policy. As mentioned in Chapter Three and Five, the arbitrators are only required to apply the applicable law to both the arbitral agreement and the contract without giving any consideration to the public policy regarding a conflict of laws. Such confusion would lead to more conflicts

between public policies. The exception of public policy under the NYC can be considered only by the enforcement court. However, such public policy should be the public policy of the country where the enforcement award or part of it is sought, not just under the place of enforcement. Art V (2) (b) of the NYC is not clear in this aspect. It is likely to be the country who issued the order of the enforcement of the arbitral award or else the country in which such award will be enforced. Logically, is the latter because in the event of actual enforcement of the award it will be in protection of the interest of said country's own interests.

6.3.2.1 Arbitrability and public policy

Most countries have a non-arbitrable concept based on both the violation of public policy and substantive law (see Chapter Five). A breach of public policy may not be a breach of mandatory rules. However, a violation of mandatory rules may be interpreted as breaching public policy.¹⁰¹⁵ Non-arbitrable awards are not enforceable under Art V (2)(a) and an award is only non-arbitrable if it was the result of a matters that cannot be settled by arbitration. The award would be refused if it is contrary to the public policy, including non-arbitrable matters. In addition, such a matter may also be considered under the applicable law to arbitral agreement under the seat of arbitration. Either a clear definition of both the concept of public policy and non-arbitrable matters must be given, or else only one of these should be kept as grounds for refusal. To avoid duplication, there are those who observe that it is appropriate to revisit the matter of public policy as a requirement of enforcement of arbitral awards.¹⁰¹⁶

6.3.3 Public policy and mandatory rules

This has led to a discussion of whether public policy deserves more attention for practicability in international commercial arbitration or whether mandatory rules must be given priority. Often, national courts have held that the mandatory laws and rules reflect public policy.¹⁰¹⁷ Such an approach is also considered through the application of international public policy.¹⁰¹⁸ Thus, mandatory rules are preferred as they promote public interests. The same approach can be found in transnational public policy. The application of mandatory rules in transnational public policy is based on the test of shared values.¹⁰¹⁹ According to Racine,

¹⁰¹⁵ See e.g. Mistelis and Brekoulakis 11–34; ‘Russia’s Mistral Deal under International Sanctions—will the Dispute Be Arbitrable?’ (*LexisNexis*, 2014) <<http://blogs.lexisnexis.co.uk/dr/russias-mistral-deal-under-international-sanctions-will-the-dispute-be-arbitrable/>> accessed 18 October 2015.

¹⁰¹⁶ See e.g. Albert Jan van den Berg, *New Horizons in International Commercial Arbitration and Beyond* (Albert Jan van den Berg ed, Kluwer Law International 2005) 287–291.

¹⁰¹⁷ Born 3327; Szaboles Balazs Szboles Steiner and Tibor Varady, *Public Policy as Ground for Refusal of Recognition of Foreign Arbitral Awards with Special Focus on Austria and Hungary* (CEU, Budapest College 2012) 14–30.

¹⁰¹⁸ Henriques and Advogados; Zekos 44–45; Savage and Gaillard 853.

¹⁰¹⁹ Marc Blessing, ‘Choice of Substantive Law in International Arbitration’ (1997) 14 *Journal of International Arbitration* 39, 61.

transnational public policy works at the same level as the mandatory rules approach.¹⁰²⁰ However, transnational public policy differs in style from the application of the mandatory rules of the state.¹⁰²¹ According to Fouchard, to apply mandatory rules there are two steps; first determine the basic policies of the applicable law and second, clarify the relationship between applicable law, the issue of dispute, and the implications of their application.¹⁰²²

The mandatory international rules, such as the freedom of the parties in international contracts, are acceptable globally whether between individuals or entities in accordance with Article 9 of the decisions of the Institute of International Law for 1991.¹⁰²³ The freedom of the parties that is considered as a substantive mandatory rule in the international community may be accepted by all States and taken into account. It should be ignored since this theory will not contribute to the resolution of disputes, specifically in contracts involving usury, and which also may be considered mandatory provisions. It will also open up more disputes at the international level and will become a thorny issue by creating conflicts between laws,¹⁰²⁴ raising problems with respect to the applicable law and the law of the place of enforcement. It seems that the mandatory rules of the law of the place of enforcement are worthwhile to consider, as are those related to public policy of the state. The law applicable to the arbitral agreement or to the contract and merit of dispute may also have an influence.

Conflict is not limited to mandatory rules but also to the substantive mandatory laws, especially with regards to the awarding of usury. There seems to be confusion about the distinction between mandatory rules and mandatory laws. Awarding interest or usury in one country is considered substantive, and in another is considered procedural depending on the type of such matter (see Chapters Four and Five). With respect to the contract in a country that considers interest-based loans to be substantive matters, the mandatory laws that cannot be overridden by the contract of the parties.

Steiner has listed substantive public policy rules and procedural public policy rules,¹⁰²⁵ but in fact these rules may be also considered substantive and procedural mandatory rules. However, most such rules are internationally agreed upon, especially the substantive rules that are related to contracts. They are not the main issue that affect the enforcement of foreign arbitral awards under public policy, but only for arbitral awards related to substantive mandatory laws. The international or transnational public policy may not be sufficient to unify such mandatory

¹⁰²⁰ Racine 767.

¹⁰²¹ Savage and Gaillard 852.

¹⁰²² Savage and Gaillard 852; Born (n 22) 2714.

¹⁰²³ PL Landolt, *Modernised EC Competition Law in International Arbitration* (Kluwer Law International 2006) 124.

¹⁰²⁴ Whether should be considered the parties autonomy more than the matter of the dispute and the law of the court or the public policy of this country or not, does the international or the transnational public policy more important than the public policy of the country.

¹⁰²⁵ Steiner and Várady.

laws with regard to conflicts in contracts that include interest. They will also result in a similar conflict in these countries in accepting the international or transnational public policy at the expense of national public policy. In addition, the laws of usury are changeable in some countries, and there is difficulty in ignoring these laws in order to accept the international or transnational public policy where they do not cover the matters of interest in general, or when identifying procedural and substantive laws in this regards.

Baniassadi discussed the three problems faced in the application of mandatory laws of public policy in the wake of international arbitration conventions.¹⁰²⁶ First, there arise ambiguities among parties that the mandatory laws in public policy would introduce unnecessary interference in performing and implementing the international arbitration contracts. Second, public policy is constructed with a focus on local values and social terms but the contracting parties see enforcement of contract laws according to international conventions that are acceptable to all. Third, in the mechanism with which the arbitral award will be enforced. Baniassadi discussed these problems through the whole arbitration process, but public policy should only take into account the enforcement of a foreign arbitral award stage under Art V (2)(b) of the NYC.

Mandatory laws in international arbitration give affect in three places or stages: in the recognition and enforcement of the arbitral agreement under its applicable law, in the recognition and enforcement of the contract under its applicable law, and in the recognition and enforcement of the foreign arbitral award under the law of the enforcement country (see Chapters Four and Five). In the first stage the arbitral agreement should be recognized and enforced unless it does not exist or the matter is not capable of settlement by arbitration, although all commercial matters are arbitrable under the mandatory rules. In the second stage, the contract is enforceable unless it is contrary to substantive mandatory law, if it is not the mandatory rules take place under the applicable law. The stage or place most closely related to the mandatory law is the place of enforcement of the arbitral award, whether under the arbitrable or public policy.

The questions of non-arbitrability are decided sometimes under public policy and sometimes under the mandatory matters, whether substantive or procedural (see Chapter Five). However, the procedural matters are reviewed at the request of the party, while the substantive matters are considered under the law of the place of enforcement. As a result, both the violation of public policy and non-arbitrability are considered under national law. Thus, awarding usury or illegal interest is contrary to the substantive mandatory law, whether consider as non-arbitrable or against public policy.

¹⁰²⁶ Baniassadi. He discussed the case of *Mitsubishi v. Soler Chrysler-Plymouth* 473 U.S. 614 (1985) *Mitsubishi v. Soler Chrysler-Plymouth* 473 U.S. 614 (1985), 83-1569 473 U.S. 614 (U.S. Supreme Court 1985)

Some countries may consider procedural mandatory law as part of public policy, thereby violation of such law may be contrary to public policy. For example, s.4 of the England Arbitration Act states, 'The mandatory provisions ... have effect notwithstanding any agreement to the contrary'.¹⁰²⁷ However, such provisions may take effect regardless of the mandatory rules. The overriding of mandatory rules and procedural law takes place when a conflict meets judicial proceedings. Mandatory rules sometimes adversely affect procedural justice. Governments prefer to adopt justice systems with the least cost for the plaintiff and earliest possible justice to the people. Often, as is the case with United Kingdom, mandatory rules are compromised for the sake of agile justice. In the 'Rules and Practices Directions', there is a provision that empowers the judiciary to manage cases hastily.¹⁰²⁸

6.4 Conclusion

In practice, there are different interpretations with regard to public policy such as international, transnational or national public policy and it may include both procedural and substantive matters. Public policy is a dynamic concept that involves political, social, cultural, moral, and economic dimensions, to meet the changing needs of an individual society. It is difficult to give a uniform definition, as it is a wide-ranging concept. It has connections to morality, basic principles of law, mandatory rules, fundamental rules of justice, the protection of national interests and foreign relations; and the main source of law is also an indicator of public policy. With the different concepts of public policy, it is difficult to identify these dimensions within the international and transnational scale. Some rules and principles of national public policy constitute categories of the concept of international public policy, such as the principles of freedom of the parties, good faith and other principles and rules that are internationally agreed. Any breach of the provisions or the choice of the law of contract will be considered a breach of international public policy according to these principles.

Many national courts acknowledge that the enforcement of public policy under the NYC requires a narrow approach with respect to public policy. Some national courts would refuse enforcement only where such enforcement would violate 'the most basic notions of morality and justice', or 'be clearly injurious to the public good'. The overlap between public international law and private international law leads to confusion in distinguishing between international, transnational and national public policy. The main cause of confusion is the difficulty of distinguishing between national and international public policy. However, the concepts of

¹⁰²⁷ Arbitration Act 1996.

¹⁰²⁸ 'OVERRIDING OBJECTIVE' (*Ministry of Justice, UK, 2015*) <<http://www.justice.gov.uk/courts/procedure-rules/civil/rules/part01#1.4>> accessed 19 October 2015.

international public policy and national public policy inevitably overlap with each other within the area of law similarly to the transnational concept.

Usury and interest issues pose a dilemma when applying the concept of public policy, where they vary from one law to another. Even the concept that is applied by France and some other countries varies according to its interpretation and application, where the award that contains interest should not exceed the illegal interest rates in the foreign State. In the case where Saudi Arabia is chosen as the seat or if *Sharia* law is the law governing the dispute, no interest can be tolerated. The application of international public policy by the French court is only an exception compared with most other jurisdictions which share no unified rules or laws regarding interest on the international scale and one sees various interest rates operated. Charging above the national interest rate is illegal, as it is substantive in the view of some national courts. International public policy does not distinguish between procedural or substantive rules as it is meant to provide protection to the national public policy of the enforcing states. Unless laws on interest were consolidated globally, which would require a tremendous amount of effort, there would be a space for national public policy.

The lack of definition of Art V (2) (b) leads to a general and confused concept which offers the signatory countries a loophole to exercise their discretion in rejecting awards containing interest. Without a unified interest rate or a consensus on the nature of interest among the signatory countries, theoretical enforceability of NYC awards will not see the signatory countries in practice observe their duty in enforcing awards made in other signatory countries. Consequently, national law is responsible for the protection of the interests of the country which determines the rules of justice and protects the sovereignty of a state. Consequently, one sees three meanings of public policy being applied: first, the concept of international public policy under the French approach, second, rejecting the enforcement of a foreign arbitral award that includes interest under national public policy only if the applicable law to the dispute is of the enforcing court, as practised by Egypt and UAE, and third, limiting the matters only to what constitutes a violation of substantive law of the enforcing court as practised in the USA, Saudi Arabia and partially in the UAE.

However, the research has shown that the application of national public policy did not ignore the interests of the international community or other countries, as most countries take into account the interests of other signatory countries, providing that it is compatible with their own national interests or national laws. Furthermore, the terminology of 'international' under the NYC does not necessarily refer to either the international or the transnational public policy, but only refers to the arbitration that takes place in different countries and contains a foreign element.

A relationship between public policy and national law, and between mandatory, substantive and procedural rules, can cause complications which arise from the interrelation of public policy and substantive rules, i.e. the public policy may include substantive rules and the substantive rules may include public policy. Procedural matters should not be considered as public policy matters, as this will result in over-expansion of the concept of public policy. From the research, it appears that public policy in Saudi Arabia and other Islamic countries is ambiguous and needs further clarification, whereas the UAE is relatively liberal but provides no black letter approach on the concept of public policy. The most undesirable situation in the matter of interest is the interlink between the substantive law and public policy. Without any further clarification on this matter, violation of the substantive law will be viewed as the main reason for refusal of the enforcement of a foreign arbitral award by some countries, in order to provide a balance between the enforceability of arbitral awards and the protection of the said countries' own interests. In other words, enforcement of foreign arbitral awards with the violation of substantive laws should not be refused unless the law of the place of enforcement is expressly applicable to the dispute, or the performance of the obligations is carried out in the enforcing state. In this way, an amicable international arbitration standard can be maintained.

Chapter 7. Conclusion

The enforceability of the foreign arbitral award containing interest in international commercial arbitration under NYC is affected by many factors and different interpretations under different laws and legal systems. The effect is present from the first step of the arbitration process till the enforcement of such award due to the diversity of the interest and usury laws under different countries. There are many potential areas of conflict in the settlement of international arbitration disputes. For example, the conflicting laws arise in the international arbitration process under seat of arbitration through the application of the law relevant to the dispute, and in the enforcing the award in the enforcement place. Another conflict can arise between the law applicable to the arbitration agreement and the law of the seat of arbitration regarding the validity of the arbitration agreement and the determination of the non-arbitrable matters. Where the arbitration agreement is an arbitration clause, the law applicable to the contract could be also in a conflict with these laws with respect to the validity of the arbitration clause.

In the case where a conflict arises between the law of the arbitration seat, the law that governs the arbitration agreement and the law applicable to the contract in the jurisdiction of the arbitral tribunal in the scope of the arbitration in case that the parties do/do not agree on the interest rate and period. Another case where a conflict can occur is between the law governs the contract, the law governs the arbitration agreement, and the the law of the arbitration seat in the determination of substantive law govern the dispute including interest or usury, also in the application of such law. Finally, a conflict also arises between the law of the enforcement place, the law applicable to the contract and the law of the arbitration seat in enforcing the foreign award that contains interest or usury under the non-arbitrable matters and under the violation of public policy.

In addition, in some jurisdictions, there are limitations on the freedom of parties under the substantive national law and the public policy of the arbitration seat with regards to submission of their disputes to arbitration, under the law governing the arbitration agreement in choosing the law to govern their disputes, under the law governing the contract and disputes with regards to choosing and applying their clauses to the contract, and under the law of enforcement place in enforcing the award according to their agreement. Such limitations would also extend to another dimension that covers the freedom and the authority of the arbitral tribunal to determine the non-arbitrable matters, the validity of the arbitration agreement and the contract, and the scope of the arbitration, also when applying the appropriate laws or rules to the dispute.

Regarding interest disputes, the main reason for refusing the enforcement either of the arbitration agreement, the arbitral award, or the the clauses of parties to the contract is the violation of the substantive law of either the law of the seat of arbitration, the law applicable to

the contract or the law of the enforcement place. In addition, the violation of the substantive and procedural rules of the law of either the seat of arbitration, the law of the arbitration agreement or the law of the main contract, with regards to the validity of the arbitration agreement or the validity of the main contract. Further, violating the procedural rules of either the seat of the arbitration or the law governing the arbitration agreement during the arbitration process may lead also to rejection of enforcement of the arbitral award at the request of a party.

Most countries have the same hesitations when it comes to applying a foreign law and delegating authority to the arbitrator in the enforcement of a foreign arbitral award under foreign law. In most jurisdictions, awarding interest or disputes containing illegal interest rates under the violation of the substantive law, is directly related to non-arbitrable under the subject matter of dispute, or public policy, whether under the seat of arbitration or under the enforcement place according to the meaning of Art II (1) and Art V (2) (a) and (b). Some countries would reject enforcing clauses of parties when interest is involved if such clauses are contrary to the substantive law under law expressly applicable to the dispute, according to Art V (1) (c) of the NYC. The awarding interest would also be unenforceable according the procedural rules regarding the scope of arbitration if the parties agree or not on the interest rate and period in the meaning of Art V (1) (c). A clause containing illegal interest would be a violation of the substantive rules and affect the validity of the contract or the arbitration clause according to some jurisdictions' interpretation in the meaning of Art II (3) and Art V (1) (a).

7.1 Interest and usury with regards to substantive and procedural law

Interest and usury laws vary from one country to another according to its law or the legal system it is based upon. Usury is a substantive matter in most jurisdictions, where charging above the legal interest rate on a loan is considered a violation of substantive law of these countries. Such interest rates are changeable and different from one country to another. In most countries compound interest is not allowed and it is contrary to the substantive law. In some countries, interest in compensation or late payment a substantive matter while in others it is a procedural matter. The case is the same for the pre-judgment and post-judgement decisions regarding the period of interest charged in compensation and late payment. Under the Common Law countries, the waiver of legal right for minimum interest is considered a violation of substantive law in some circumstances, while the waiver of lost profit in breaches contracts or other damages matters is procedural matter.

In Saudi Arabia an interest-based loan, even at low rates, is considered *Riba*, which is prohibited. This is considered a substantive law according to *Sharia* law, whether under the application of its law or in the enforcement of the award that contains *Riba*. However, with respect

to compensation it is considered that not every award containing interest is *Riba* under *Sharia* law. Regardless of how the concept of usury or *Riba* are used here, the illegal interest rates in loan contracts are not acceptable in many jurisdictions. Interest-based debt resulting from late payment is not subject to usury law in most countries, and in Saudi Arabia it is considered *Riba* under *Sharia* law. Such prohibition is only related to the loan contract under the parties' agreement, but interest upon late payment is not prohibited with regards to the sale of goods or services contracts under the parties' clauses. Compensations in all commercial activities for breaches of contract or late payment are allowed under *Sharia* law in case there are damages, and such compensations are applied equally to the actual damages even if there is no agreement. However, compensation for any other damages is considered procedural unless it is compensation for late payment, when it is considered substantive under *Sharia* law.

In England there is a minimum interest rate for loans or late payments and the Acts regarding unfair terms refer to unreasonable clauses that would be against its substantive law. Unreasonable clauses are not defined under English law, but may refer indirectly to fraud or bad faith. In addition, there is no limit or cap for the interest rate in the Arbitration Act 1996, which allows for simple or compound interest applied over any period. Although disputes over high interest rates do not constitute a violation of substantive law of English law, the parties' autonomy and the authority in determining and applying the interest rate is wider than in other countries under the Arbitration Act 1996. Compensations under English law are limited to the actual damages, and the interest rate on late payments is applied directly as an implied interest if there is no agreement. English law is stricter in awarding damages. In international arbitration, English law is not applied directly unless it is subject to the closest connection test with regards to the place of obligations and business etc. Enforcing a foreign arbitral award containing compensation or a high interest rate under a foreign law does not also constitute a violation of public policy when the enforcement place is English.

In the U.S., illegal interest or usury constitutes a violation of the substantive law, whether in the application of the law or in enforcing a foreign arbitral award containing illegal interest when the enforcement place is the U.S. However, the Federal law does not address illegal interest or usury, so it is difficult to determine the legality of the interest under the law of the enforcing court where each state has its own usury law. Thus, there are variations in interpretation of public policy in the U.S. when a substantive law is violated. Compensations are procedural matters in the U.S. for breaches of contract, but the parties must expressly determine the interest rate and period for actual damages, and the late payment terms in the parties' clause/s should be reasonable. Here, the definition for the unreasonable clauses are clauses that contain fraud, which is against a strong public policy of the forum. Generally, in most cases the foreign arbitral award

as compensation under a foreign law is enforceable in the U.S. as a procedural matter. However, the court in some cases intervenes in setting the interest rates and period.

In Egypt and UAE, charging illegal interest rates or ones contrary to the usury law constitutes a violation of substantive law of both countries. For both, the interest rate in commercial loans differs from civil loans, but in UAE interest-based civil loans are more limited and their prohibition is unclear under UAE law. Compound interest is contrary to Egyptian law as charging compound interest constitutes a violation of the substantive law of Egypt, while in UAE the law is less consistent in this regard. The late payment is subject to a maximum interest rate in Egypt, while in UAE it is not. The compensation matters are procedural matters in both countries, but in UAE it is a more flexible matter. A foreign arbitral award that contains illegal interest is in both countries unenforceable as it violates the substantive law of each country' law as well as public policy, unless such award was governed by a foreign law.

In France, as in other countries, charging illegal interest rates or violating the usury law is contrary to the substantive law of France when French law is applied. However, in international arbitration, the foreign arbitral award containing interest is enforceable in France unless such award containing interest rate is contrary to the maximum rate of the law of the foreign country. France adopts the concept of international public policy when rejecting the foreign arbitral award, where any award should not be contrary to the international public policy. Most Civil Law countries adopt such a concept, but with a different interpretation in this regard.

7.2 The freedom of parties

The freedom of parties to enter into a contract and organize their obligations are recognised under all legal systems, national and international laws. However, such freedom is limited by mandatory rules, where the mandatory rules are those that cannot be detracted from an agreement. The mandatory rules protect the social and economic interest of the country, overriding the mandatory rules leaves the contract null and void. Such rules are applied even if the contracted parties attempt to override or modify them. The public law of the national law is mostly constituted of mandatory rules. Civil Law codes are mandatory rules, and in *Sharia* law the matters that are prohibited by *Sharia* law are mandatory rules.

The parties must negotiate and perform their contract in good faith or it would otherwise be unenforceable. The parties' clauses to the contract is enforceable according i.e. to the principle of *pacta sunt servanda*. However, unfair or unconscionable clauses or contracts containing usury that are designed to achieve an illegal objective are void or at least unenforceable. In arbitration, most national arbitration laws allow the parties to choose the law, rules or a legal system, where they leave ample room for party autonomy. The party autonomy is more general when making

the contract and determining the law, clauses etc. The party autonomy with regards to interest-based contracts under the clauses of the parties is limited by either non-arbitrable matters, the validity of the contract, the law applicable to the contract or by public policy under the enforcement place.

The parties' choice of law replaces both peremptory norms and mandatory rules of the law that would be applied by national court. In the international arbitration disputes, the contract is enforceable by the arbitrator by relying on the applicable law to such contract, and the court of the enforcement place shall only consider the foreign arbitral award to ensure: first, at the request of the parties, that the law applicable to the contract has been applied properly according to ; and second, that such a foreign arbitral award is based on the applicable law and does not conflict with public policy of the enforcement place.

7.3 Existence Arbitration agreement

The existing arbitration agreement must be treated as it is valid, unless there is a glaring defect. Arbitration agreements are binding on the parties, arbitrators and on the courts, where it reflects the desire of the parties to submit their dispute to arbitration. As a result, it takes the dispute out of the jurisdiction of the courts and to arbitration (under the jurisdiction of arbitral tribunals or arbitrators). Such arbitration agreements determine the authority of the arbitral tribunals or arbitrators with regards to the parties' clauses, the application of the law governing the dispute and the scope of the arbitration. The express law to the arbitration agreement is the law determines the non-arbitrable matters, the rules of the validity of the arbitration agreement, and the scope of the authority and jurisdiction of the arbitral tribunals or arbitrators in determining the scope of arbitration, the validity of the arbitration agreement and awarding interest in absence of the law applicable to the dispute or the clauses of parties in such regard. In addition, it is the law that determines the procedural rules and arbitration process.

If the parties fail to choose a law applicable to the arbitration agreement where the arbitration agreement is independent from the main contract, the law of the arbitration seat is the law applicable to the arbitration agreement as the implicit choice. It also appears there is a difference between the facts whether the arbitration agreement is connected or separated. The express law applicable to the contract that is dependent on the arbitration clause is the law that governs such arbitration agreement, otherwise if the parties do not agree under the express then the law of the arbitration seat is applied implicitly if the parties have expressly identified the seat; if the seat was not identified then the law is applied as it deems appropriate. According to Art V (1) (a) (d) of NYC, where the law applicable to the arbitration agreement or the contract is still the law that is chosen by the parties, otherwise the law of the arbitration seat is applied. Some

national arbitration laws such as the English Arbitration Act and the Saudi Arbitration Law apply automatically to the arbitration when the parties expressly choose the seat of arbitration. The priority in the law applicable to the arbitration agreement is to the law of the seat of arbitration, in the case that the parties have explicitly chosen such a seat. However, such arbitration laws should not give effect where there is an express law to the arbitration agreement to avoid such a conflict. The law applicable to the arbitration agreement implicitly provides the same functions of the express law.

Judicial intervention affects the arbitration process where there is no jurisdiction for the arbitrators under the applicable law to the arbitration agreement. Thus, if review of the arbitration agreement is necessary, action should be taken before starting the arbitration process and issuance of the arbitral award. The invalidity of the underlying contract does not automatically extend to the arbitration clause in this contract (i.e. applying the principle of separability). The enforcement court should not rely on parties' requests in the scope of arbitration as grounds for refusal where a valid arbitration agreement and a general or specific authority has been given to the arbitrators. As a result, such an agreement includes either disputes that have arisen or will arise. According to the authority of the arbitrators, such disputes can be considered by the arbitrators under the law applicable to the contract, whether the parties have agreed to their clauses with regards to interest rate and period or not.

7.4 The dispute and interest/usury

The parties' dispute in arbitration involving usury or illegal interest according to the parties' clause is considered under some jurisdictions, under the seat of arbitration, as non-arbitrable according to the interpretation of Art II (1) of the NYC. Such action leads to the rejection of enforcement of the arbitration agreement according to a violation of substantive law and public policy. However, in fact this article refers only to the subject matter of the dispute that is not eligible for settlement by arbitration, which indeed refers directly to the disputes that cannot be settled by arbitration, such as criminal or personal status disputes according either to the law applicable to the arbitration agreement or otherwise according to the law of the arbitration seat. In addition, it refers indirectly to the disputes that require approval from the competent authority to enter into arbitration agreements, which is determined by the law applicable to the arbitration agreement, for example with administrative contracts. Bankruptcy matters related to late payments are arbitrable only if the law requires that the parties cannot enter into the arbitration agreement without prior approval from the competent authority, so it affects the capacity of the parties to enter into an arbitration agreement. Such action is logically incurred only if one of the parties in arbitration has faced bankruptcy before entering into the agreement and it does not apply to the arbitration clause. In brief, non-arbitrable matters are related only to either the type of the

dispute or approval of an arbitration agreement. In general, interest disputes are arbitrable where commercial disputes are arbitrable. These matters could be considered by the arbitrators under the applicable law to such disputes.

Arbitration agreements typically include a choice-of-law provision addressing the substantive law applicable to the dispute, which more broadly governs their entire relationship including their obligations, good faith, and capacity. Such law is the law determines the validity of the contract. In arbitration, the parties' contract is enforced by the arbitrator under the applicable law to such contract. In some countries, the award would be set aside or suspended if the arbitrator fails in the application of the law applicable to the contract, or would be considered outside the scope of arbitration when the merits of dispute are considered by the arbitrators without giving consideration to the parties' clauses, especially if their clauses refer to interest rate and period. The law of the arbitration agreement and the law of the seat of arbitration would give effect under some jurisdictions, and lead to conflict between the law of the contract, the law applicable to the arbitration agreement and the law of the seat of arbitration, despite existence of the law governing the dispute.

7.4.1 Court interventions

Most jurisdictions intervene in the law applicable to the disputes under different unreasonable justifications, whether under public policy, non-national concept or indirectly under violation of substantive law. The law of Saudi Arabia gives adverse effect to the applicable law whether under Saudis' seat of arbitration or though applying the Saudi Arbitration Law to the arbitration agreement. It requires the applicable law and the parties' clauses shall not be contrary to *Sharia* law. The prevailing views in *Sharia* law is that arbitrators should settle disputes according to the rules of *Sharia* law and take into consideration the provisions of public policy, a reflection of the meaning of arbitration under *Sharia* law. Such a view is reasonable and acceptable where the dispute is considered under domestic arbitration and the arbitral award would be enforced in Saudi Arabia. However, applying *Sharia* law in this regard is ignoring the chosen law or the parties' agreement, and causes further conflicts between different jurisdictions. As a consequence, such intervention in the applicable law leads to a different result, though the fact that the arbitral award under the applicable law to such dispute could be enforced elsewhere is not necessarily enforced in Saudi Arabia.

When the seat is English and a court intervenes in the law governing the dispute, the closest connection test applies even if the parties have chosen an applicable law. In most cases the English law is implicitly applied as the law applicable to the dispute. The Late Payment Act 1998, Unfair Terms Acts or any other substantive obligations which arise as a matter of English law apply under the English seat. The s49 of the Arbitration Act 1996 also automatically governs

and determines any dispute involving interest. In addition, English courts ignore *Sharia* law in the case it has been chosen as the law governing the contract and consider it as non-national law, e.g. *Shamil Bank* case. Thus, in all cases applying a different law to the dispute results in a different outcome. In this case, in *Shamil* this part of the contract was unlawful and unenforceable under *Sharia* law as it included *Riba*. However, the action of the English seat in *Shamil* was mistaken for many reasons. Briefly, *Sharia* law was the law that was chosen expressly by the parties to govern their contract, *Sharia* law is a law that is applied in different countries according to its resources and rules and can be used globally, the concept of *Riba* could be identified in the case, the case could be considered and discussed by qualified arbitrators, and in fact *Sharia* law is the national law of Saudi Arabia, where it can be interpreted if it is necessary.

In general, under a perceived ambiguity, the Common Law shares the same ambiguity with *Sharia* law in some aspects, such as when it is difficult to be interpreted by foreign arbitrators and judges and when the disputes need to be considered on a case-by-case basis. Furthermore, the Rome Convention would not be applied to non-contracting States in most cases. Even Rome II also does not apply if the contract is closely connected to the law of another state under Art 4 (5), though, this Convention is not in line with the NYC with regards to the applicable law. In contrast, the Rome Convention refers to the freedom of choice of law governing the contract, and such contract shall be governed by the law chosen by the parties according to Art 3. In fact, English law also recognises the freedom of the parties to choose the law that governs their contract and the clauses defining interest rate and period. Under s49 of the Arbitration Act the arbitrators can make an award with regards to interest rate and for any period where there is no agreement on this matter. The agreement on the interest rate and period can be governed together by the chosen law and the clauses to the dispute, or in the event there is no agreement at least one of them can be used with the absolute authority of the arbitrators. The law chosen by the parties in all cases is still the parties' choice, and the parties expressly want such law to govern their dispute.

Court intervention leads to a conflict between the law governing the contract, the law of the arbitration seat and the law applicable to the arbitration agreement. In international arbitration, neither the seat of arbitration nor the law applicable to the arbitration agreement is more important than the law applicable to the dispute. Such law is the law that gives effect to the outcome of the award. No law should give effect to the dispute if there is a law in existence to govern such a dispute. The chosen law would determine the legality of parties' clauses, which depends on whether such chosen law contains restrictions on the freedom of contract, allows these clauses in the contract, or if there are restrictions on the ability of the parties to pay the interest. Such a law also governs the validity of the contract, the capacity of the parties and all of the matters related such as the bankruptcy matters. A clear and accurate law applicable facilitates the arbitration proceedings and avoids further conflicts.

7.4.2 *Determination the applicable law*

There are many arguments with regards to the law applicable to the contract in the event that the parties fail on the choice of law of the contract or the interest rate. In absence of a chosen law, it would be more complicated where the applicable law may be subject to several conventions, laws and trends such as the Rome Convention and the principles of private international law. This process may contribute to a slow down in the arbitration, breaking confidence and leading to many conflicts with regards to invalidation of the arbitration agreement, the determination of interest rate and period and the determination of the substantive and procedural matters. Conflicts have arisen between the law of the arbitration agreement and the law of the seat of arbitration in the absence of a law governing the contract containing interest. Some countries apply the choice of law rules to determine the law applicable to the contract and dispute. In England, the law applicable to the contract is determined by testing and interpreting the contract if the law was chosen implicitly or not. In absence of a chosen law, either expressly or implicitly, the applicable law is determined by reference to the Rome Convention and testing the proper law of the contract. Under such a test *lex fori* is the law that governs procedural matters, while the substantive matters are governed by *lex contractus* or the place of performance of the obligations arising under the contract etc., by using the closest and most real connection test. In the U.S., the approach is similar to England, but in most cases in the determination of substantive and procedural matters, the law of the arbitration seat is applied. In Egypt and Saudi Arabia, the law of the arbitration seat is usually applied, without applying the conflict of laws rules unless the parties are agreed. In France, whatever decision was made by arbitrators in the determination of the law applicable to the dispute is applied unless it is contrary to mandatory rules.

The law applicable to the contract should be determined according to the indication of Art V (1) (e). However, according to Art V (1)(e) of NYC, it could be set aside or suspended under that law if it gives effect to the merit of dispute. Sometimes the court of the chosen law, whether expressly or implicitly, intervenes to ensure that the law is applied properly to the dispute, into account the law governing the contract, especially the substantive law with regards to the merit of dispute. Ignoring such a law may result in rejection of the arbitral award in the end. As a result, the award would not become binding or would be set aside or suspended under the chosen law or under the arbitration seat. However, according to some interpretations and examinations of the purpose of this Art, it appears that the Art refers to the law applicable to the dispute, were Art V (1) (a) refers to the law applicable to the arbitration agreement and Art V (1) (d) refers to procedural matters of the arbitration. Thus, the law applicable to the dispute determined according to Art V (1) (e) will be in favour of international arbitration and the unification of the rules. Three

laws are at play in this regard, the law applicable to the arbitration agreement, the law governing the dispute, and the law of the arbitration seat.

When there is no express law governing the contract, the law of the arbitration agreement gives effect to the law applicable to the dispute, where some arbitration laws directly provide rules to award interest or make general provisions to determine the applicable law to the disputes or the authority of the arbitrators. In this case, with the lack of express law, the parties' choice of law for the arbitration agreement is the one law governing their dispute. Some laws refer directly to awarding interest, for example, s48 and s49 of the Arbitration Act 1996, and can be applied to the dispute. Other laws require considering the national law, such as Saudi law, where the substantive *Sharia* law is in the end applied. Under some arbitration laws, the arbitrators consider the dispute as deemed appropriate, for example French law if the arbitration seat has been chosen according to mandatory rules. Likewise, other countries refer to substantive laws and public policy. The seat of arbitration here should not give effect unless is it the seat of the same law. It is not logical that the law applicable to the dispute is determined under the law of the arbitration seat, where such a law would conflict with the arbitration law. In case there is no express law governing the arbitration agreement, the law of the chosen arbitration seat is the law applicable to the contract. The arbitration law of some jurisdictions applies automatically to the seat, such as Saudi arbitration law and English law, whether or not the parties have chosen these seats. As a result, the action can be applied the same as in the previous case.

The law of the arbitration seat may perform the same function and replace either or both the law applicable to the arbitration agreement and the law applicable to the contract in the event no law(s) had been chosen. It should be treated as a law applicable to the contract, unless the parties have not agreed to the arbitration seat. It depends whether the arbitrator is obliged to apply the rules of conflict, which will depend on the law of the seat of arbitration. In most countries, if the seat has been chosen, the award should be not contrary to the substantive law of the seat of arbitration. In an Egyptian seat, Egyptian law is applied. Where there is no explicit law governing the contract or law governing the arbitration agreement, the contract and the whole arbitration process are governed by the law of the arbitration seat. The determination can be made by the arbitrators themselves, otherwise if none have been appointed then by the court of the express seat. However, it is not necessary that the seat of arbitration has been expressly chosen, where such law may be determined by the arbitrators themselves.

7.4.3 *Awarding interest*

The express law applicable to the contract is the law that governs the interest dispute and the validity of the parties' clauses in this regard. If there no clauses, the implied provisions are applied. In case there is a law applicable to the arbitration agreement, such law determines the

jurisdiction of the arbitrators to set the scope of arbitration, the validity of the arbitration agreement, and the limitation of applying and awarding interest on the contract. In absence of an express law applicable to the contract, the law applicable to the arbitration agreement is the law that determines the authority and jurisdiction of the arbitrators to award interest or not whether it deems appropriate, or considers applicable or closely connected, taking into consideration the parties' agreement. Awarding interest depends on the power and the authority of the arbitrator according to the agreement of the parties, whether general or specific authority has been given by the parties. The authority of the arbitrators is determined by three factors, in order of precedent—the law applicable to the dispute, the law applicable to the arbitration agreement and the parties' agreement.

There many arguments with regards to whether or not the arbitrators should apply the procedural laws of the seat and the substantive laws of the governing law. This approach is difficult in some aspects. The parties' agreement may not be perfect in all cases, such as in the choice of the law applicable to the dispute, the law applicable to the arbitration agreement and determining the seat of arbitration. These laws have different approaches and conflict with each other. Ideally, an applicable law would govern only substantive matters and would not be in conflict with any others. Procedural matters are determined by the law of seat of arbitration, so a conflict arises where this is different from the law of the arbitration agreement. The determination of substantive and procedural matters is difficult in some cases where a matter may be considered as procedural according to the law of seat of arbitration, but is not under the law governing the dispute, and vice versa. Practically, a matter may be considered as substantive under the seat of arbitration, but in fact it is procedural under the applicable law such as in damages disputes. If the matter is considered substantive under the seat of arbitration, it leads to the law applicable to the dispute being ignored and causes the award be set aside, or else under the applicable law to the dispute thereby making all considerations under this law. In case of failure to identify the arbitration seat, it may be said that the arbitrators choose the seat that is considered appropriate, but it is possible where this decision would meet the same effect as above with regards to the determination of substantive and procedural matters. Furthermore, it is possible that the parties leave this choice to the arbitrator in some cases where there is no law chosen nor has a seat of arbitration been identified.

Interest disputes are considered under the substantive and procedural rules of the law expressly chosen by the parties. For example, if there is no choice of law for the contract, then the law applicable to the arbitration agreement is in effect and the arbitrator has the authority to determine one based on the closest connection to the place of performance of the obligation or as it deems appropriate taking into account the parties' clauses and all considerations. In absence of these laws, the disputes are considered under the seat of arbitration as it deems appropriate

according to the parties' clauses and taking into account the substantive rules of the arbitration seat in case it has been chosen expressly. Otherwise, the arbitrators issue the award as deemed appropriate.

7.5 The enforceability of awarding interest

Art V (2) (a) and (b) of the NYC constitute the main two grounds for refusing the enforcement of foreign arbitral awards under the place of enforcement, where such grounds are considered under the law or the public policy of the place of enforcement. Most countries interpret these articles differently and always the interpretation is not in favour of international arbitration. The finality of the award depends on the interpretation given by the enforcing court, especially on the grounds of public policy. According to Art 31 of the Vienna Convention on the Law of Treaties, 'a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose'. In accordance with some countries' interpretation and practises with regards to Art V (2) (a), awarding illegal interest violates the substantive law and public policy it is considered non-arbitrable. The violation of substantive law and public policy with regards to awarding interest should not consider under this article. A violation of public policy would be considered under Art V (2) (b) of the NYC. It says that awarding interest is unenforceable if such award is contrary to public policy under the place of enforcement. This article does not mean the award itself, but rather the subject matter of the dispute that the award is based upon. The non-arbitrable concept under Art V (2) (a) is also considered under the same meaning under Art II (1), which refers to either the type of the dispute (criminal, personal status, etc.) or the requirement of approval to enter into an arbitration agreement under the law of the arbitration agreement or of the arbitration seat, and the law of the place of enforcement. If Art V (2) (a) takes the same legal effect as Art II (1), this would effectively be re-examining the matter, which would take the settlement back to the beginning and invalidate any award.

Interest law can be subject to the law applicable to the contract if the parties have chosen such law expressly or implicitly, or it can be subject to the law of the place of performance of the obligations or even to the law of the enforcing court. The potential application of different interest laws gives negative effect to the arbitrable matters, whether they are the law of the arbitration seat or the law of the enforcing court. The concept of arbitrability in relation to interest disputes encounters different laws and interpretations. These frustrate the purpose of the NYC, which was intended to ensure the enforceability of foreign arbitral awards. It is the researcher's viewpoint that the Convention should be interpreted in favour of arbitration according to the nature of arbitration and party autonomy. Countries hostile toward arbitration give arbitrators less freedom than those that are friendly toward it due to fears over the freedom of parties in arbitration. Such

conflicts in approach lead to undesirable and varied interpretations and a general confusion between public policy and non-arbitrability. The violation of substantive laws and of public policy are used equally under the seat of arbitration and the place of enforcement. There are many common characteristics shared between the rules of arbitrability in general and principles of public policy, but in fact they are different. Public policy should only be considered under the related country and within a narrow scope.

The NYC presumes arbitral awards to be enforceable as a general rule where non-enforceability is subject to specified exceptions (including public policy), which should be interpreted narrowly and strictly. Many national courts acknowledge that the enforcement policy of the NYC requires a narrow approach with respect to public policy. However, in practice there are different interpretations with regards to public policy, such as whether international, transnational or national public policy is considered and whether or not include both procedural and substantive matters are involved. Some national courts would refuse enforcement only where such enforcement would violate 'the most basic notions of morality and justice', or 'be clearly injurious to the public good'. However, there is still an "uneasy tension" between national and international public policy. The overlap between public international law and private international law leads to confusion in distinguishing between international, transnational and national public policy. The main cause of confusion is the difficulty to distinguish between national and international public policy. The debate is likely to carry on since there are no uniform views and rules with regards to interest and rules of justice and morality, public interest, procedural and substantive matters across nations. There are some rules are internationally agreed upon, whether directly or indirectly, such as freedom of parties and good faith. Public policy in most countries is not clear but with regards to interest it is related to the law in some aspects.

The greatest influence in the refusal of the enforcement of a foreign arbitral award is a violation of the substantive law. The concept of public policy cannot be defined even if we refer to the substantive public policy because such substantive concepts include substantive rules and laws still not identified by the law. In addition, it is subject to different interpretations as an 'Unruly Horse', and it may be wider or narrower than the national law. Such law is responsible for the protection of the interests of the country and determines the rules of justice as well as the sovereignty of the state. It is impossible to be procedural about public policy, which according to some interpretations may invalidate all arbitration proceedings. Thus, the violation of the substantive law is the only reasonable reason for refusal the enforcement a foreign arbitral award regardless of the procedural mandatory law in this respect. It is necessary to keep the rights of states to refuse foreign arbitral awards according to the considerations of grounds for refusal, whether according to public policy or the law of the place of enforcement.

It is the researcher's viewpoint that the narrow concept of public policy interpretation in this regard refers to three meanings— applying the concept of international public policy, rejecting the enforcement of the foreign arbitral award that includes interest under public policy only if the applicable law to the dispute is of the enforcing court, and limiting the matters only to what constitutes a violation of substantive law of the enforcing court. According to their actions, the first concept is applied by France, the second is applied by England and Egypt, while the third is applied in Saudi Arabia, the U.S. and UAE. Despite the fact that usury is contrary to French' national public policy and also is considered a criminal offense, this does not apply with regards to international arbitration unless the awarding interest violates the higher interest rates of the foreign law. There are practical difficulties in applying the concept of international public policy, e.g. in Saudi Arabia, where usury is contrary to *Sharia* law even under low interest rates. However, mixed methods can be applied through the consideration of the applicable foreign law and the law of the place of enforcement to avoid these practical difficulties. Under public policy, enforcement of foreign arbitral awards only with regards to the violation of substantive laws should not be refused unless the place of enforcement is the country of the law expressly applicable to the dispute, or the place of performance of the obligations arising under the contract. To maintain amicable international arbitration standards, only awards inconsistent with the substantive rules of applicable foreign law should be rejected. In addition, it should not reject the whole award, only the part in violation, according to the principle of separability.

7.6 Recommendations

- 1- The researcher recommends that the rules of New York Convention should be interpreted in favour of international arbitration.
- 2- Public policy, whether national or international, should be clearly defined so that States may not reject foreign arbitral awards, especially when the place of performance of the contract is another country where the award will also be enforced.
- 3- Some of the rules of the NYC require further clarification, such as Article V (1) (c) as well as Article V (2) (a) in order to prevent further negative interpretations.
- 4- The international community should attempt to unify the laws relating to international transactions and trade.
- 5- England should recognise *Sharia* law, where *Sharia* law is relevant and applicable.
- 6- There should be a clear provision under the Saudi Arbitration Law addressing awarded interest, or preferably law that contain provisions on interest should be enacted based on *Sharia*.

- 7- The Saudi arbitration should not interfere with the express law applicable to the contract under arbitration.
- 8- The Saudi Arbitration Act can be clarified by eliminating redundant articles. Article 55 should be maintained because it provides sufficient guidance for the enforcement of arbitral awards.
- 9- Saudi Arabia, Egypt and UAE should clarify its position with regards to *Sharia* law public policy.

7.7 Further research

Further study should perhaps concentrate on obtaining the most recent court decisions and tribunal awards because this could help examine the types of interest involved and their effects in arbitration. This is especially the case in Saudi Arabia, where this might assist Saudi lawmakers in reaching a clear vision of the types of interest that should or should not be adopted.

Research could also be done on Islamic contracts with a comparative basis and study of the possibilities to make laws uniform. Such research could enhance this current study because it would provide a complete understanding of Islamic contracts under different legal systems in question from beginning to end.

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