THE RECENT AMENDMENTS TO THE ITALIAN ARBITRATION: NEW RULES ON THE LAW APPLICABLE TO THE MERITS

1. Introduction

The purpose of this paper is to assess whether the reformed Article 822 of the Italian Code of Civil Procedure ("**CCP**") is consistent with the reform's goal of making Italy a more attractive arbitral seat. The paper focuses only on the possibility for the parties to choose the law applicable to the merits of their dispute, codified in the new Article 822 CCP. It does not analyze the part of Article 822(2) CCP concerning the determination of the law applicable to the merit absent valid choice by the parties.

2. The parties' freedom to choose the law applicable to the merits before the recent amendments:

Party autonomy in arbitration is not limited to the power to submit the dispute to arbitration and to appoint arbitrators. It normally includes the freedom for the parties to choose the substantive law that applies to the merits of their dispute[1]. Indeed, most arbitration laws[2] expressly contain an "arbitration-specific conflict rule"[3] that establishes the connecting criteria by which arbitrators shall designate the law applicable to the merits and, therefore, prevent recourse to general conflict rules in arbitration[4]. These provisions recognize the importance of party autonomy as the main connecting criterion by which the law applicable to the merits is designated and require arbitrators to apply the law chosen by the parties[5], even when the law chosen is not that of a country connected with the dispute[6]. Additionally, many of these provisions use the expression "rules of law"[7], and thus, do not limit the parties' choice to "a law", understood as an exhaustive national corpus of law[8]. The former includes not only national laws, but also non-State rules[9], which may be chosen by the parties as substantive rules to govern the merits of their dispute. Therefore, the use of the expression "rules of law" is intended to broaden the range of substantive rules to which the parties can subject their relationship[10]. In arbitration, the choice of "rules of law" has the same value as the designation of a "law" (i.e., a national body of law), since these rules occupy the same place as state law in the hierarchy of sources applicable to the merits[11]. Arbitration in Italy is primarily regulated by Articles 806-840 CCP, but none of these provisions expressly recognize the power of the parties to choose the substantive law applicable to the merits[12]. Italy, after the Legislative Decree nº 209/2006,[13] and until the recent amendments come into effect, lacks an arbitration-specific choice of law rule found in most jurisdictions[14]. In fact, in 2006[15] the legislature profoundly reformed the previous rules on arbitration by eliminating the whole of Chapter IV, Title VII of Book IV of the Italian CCP (the "**2006 Reforms**") and, thus, altered the very concept of international arbitration[16]. The reform led to a "monistic" system in which the rules of domestic arbitration are applied to international arbitration, with few exceptions[17]. Consequently, the legislature also eliminated the previous arbitration-specific conflict rule contained in Article 834 CCP providing: "[t]he parties shall have the power to determine by agreement the rules to be applied by the arbitrators to the merits of the dispute or to provide that the arbitrators shall rule according to equity. If the parties do not so provide, the law with which the relationship is most closely connected shall apply. In either case, the arbitrators shall take into account the indications of the contract and the usages of the trade"[18].

Under the 2006 Reforms, and considering the absence of a specific arbitration-specific choice of law rule, all arbitrations seated in Italy became rooted in Article 822 CCP, which merely states that "arbitrators judge according to the norms of law unless the parties have authorized them by any expression to judge according to equity"[19].

The Italian legislature's failure in 2006 to introduce an arbitration-specific choice of law rule to determine the applicable substantive regime has raised the question of which conflict rule is applicable to establish the substantive law on the merits, specifically in *ad hoc* arbitrations seated in Italy[20]. In fact, only for the latter type of arbitration, the "general" rules of private international law apply, including the provisions of the Rome I Regulation, where applicable[21]. However, while the Rome I Regulation[22] grants the parties the right to choose the applicable law, it does not allow the choice of "a law" other than that of a State[23]. Consequently,

only a choice in favor of the law of a State leads to that law prevailing over otherwise applicable mandatory rules[24]. When, on the other hand, the parties choose to subject their contractual relationship to a soft law regime[25], such a choice solely determines the content of the contract per *relationem*[26]. This means that the provisions contained in the chosen soft law instrument do not override the mandatory rules of the otherwise applicable law[27]. Conversely, in cases where the arbitration is subject to institutional rules (*i.e.*, the UNCITRAL Arbitration Rules), arbitrators will have to resort to the specific conflict rules contained in the UNCITRAL Arbitration Rules and not to the EU regulations on private international law, which are not of mandatory application in arbitration and are relevant only as default private international law rules[28]. These UNCITRAL Arbitration Rules contain an arbitration-specific conflict rule[29] allowing the parties to choose "rules of law" as those applicable to the merits.

The absence of an arbitration-specific conflict rule in Italy is therefore specifically relevant in the matter of *ad hoc* arbitrations seated in Italy. For this type of arbitration, the question which remains is whether arbitrators can disregard the parties' choice of non-state law by invoking the limits imposed on private autonomy by the Rome I Regulation as the default instrument of private international law[30].

To overcome this dilemma, and while simultaneously promoting the goals of legal certainty and predictability in arbitration, it was necessary to reintroduce an arbitration-specific conflict rule in Italy[31].

3. The Italian arbitration amendment project in the Enabling Act

In November 2021, the Parliament enacted the Enabling Act of Nov. 26, 2021 nº 206 (the "**Enabling Act**")[32] to reform Italian civil procedural law with the aim of promoting "the efficiency of civil procedure[33]" in accordance with "objectives of simplification, expeditiousness, and rationalization" [34]. The Enabling Act, presented as part of the Italian "National Recovery and Resilience Plan,"[35] also authorizes the Italian Government to issue one or more legislative decrees to amend arbitral legislation in compliance with eight (8) specific guiding principles and criteria[36].

As stated in the Report[37] accompanying the proposals presented by the "Luiso Committee"[38] (incorporated into the Enabling Act), the objective of these amendments on arbitration is to "general[ly] enhance[] […] the institution of arbitration" as well as to "strengthen[] […] its specific prerogatives" in order to, "reinforce the confidence in the institution among potential users"[39]. In particular, "it is intended to conform arbitration in Italy to that provided in European rules"[40]. These statements demonstrate that the *ratio* behind the reform is to improve arbitration in Italy also in light of foreign legal systems considered more advanced in this field,[41] with the ultimate aim of "making arbitration more attractive […] to individuals and foreign investors"[42].

Next, Section d of Article 1(15)[43] introduces the express possibility for a party to choose the law applicable to the merits of the dispute. Specifically, the guiding principle requires the legislature to "provide, in the case of adjudication according to law, the power for the parties to indicate and choose the applicablelaw"[44]. As rightly pointed out in commentary[45], the formula used by the legislature in Section d is ambiguous and incomplete in some respects. First, from a terminological point of view, the simultaneous use of the verbs "indicate" and "choose" is ambiguous. On one hand the term "indicate" can refer to situations where only one option is possible, in contrast with the term "choose" which presupposes the existence of two or more options[46]. Second, the formula generates uncertainty because it does not clarify whether the reference to "applicable law" refers only to "a (State) law" or also includes the possibility for parties to choose non-State "rules of law". Finally, the formulation is silent on the test which arbitrators should apply to identify the applicable law in absence of a valid choice by the parties[47]. As detailed in the following section, some of these gaps and uncertainties have been resolved by the recent Legislative Decree nº 149/2022. However, the final formulation of Article 822 CCP, which filled the gaps in Section d[48], has also generated its own perplexities.

4. Critical remarks on Article 822 CCP after the enactment of Legislative Decree of Oct. 10, 2022 nº149

On October 10, 2022, the Italian Government implemented Enabling Act nº 206/2021 with the enactment of Legislative Decree No. 149/2022[49]. Article 3(53) of Legislative Decree nº 149/2022 finally reintroduces an arbitration-specific choice of law rule with the addition Article 822(2) CCP, which will become effective on June 30, 2023. The new provision[50] states that:[51]

"[w]hen the arbitrators are called upon to decide according to the rule of law [(*i.e.*, as opposed to equity)], the parties in the arbitration agreement or by virtue of a written instrument preceding the initiation of the arbitration proceedings may indicate the provisions or a foreign law as a law applicable to the merit of the dispute. Failing this, arbitrators shall apply the provisions or laws identified under the conflict criteria deemed applicable".

This provision introduces an arbitration-specific choice of law rule in Italy that recognizes party autonomy as the main connecting criterion. However, this new rule is inconsistent with modern approaches to the law applicable to the merits (**A**) and does not it eliminate all uncertainties when determining the applicable law (**B**).

5. The inconsistency of the new provision with modern approaches to the law applicable to the merit

In this respect, the provision has two problematic aspects. Firstly, the opening sentence of the new provision states that parties may chose the applicable law only "in the arbitration agreement or by virtue of a written instrument *preceding* the initiation of the arbitration proceedings"[52]. The legislature, in the Explanatory Report to Legislative Decree 149/2022[53], made it clear that this temporal limitation of party autonomy "responds to the logic of identifying in advance […] the applicable law" in order to "allow the arbitrators to consider whether or not to accept the appointment" and thus, avoid "[the] unnecessary waste of procedural activity"[54]. However, this limit on party autonomy is not in line with modern approaches to the parties' choice of law applicable to the merits. Virtually no other States' arbitration-specific choice of law rules have a temporal limitation[55]. It is therefore evident that such restriction is inconsistent with the goal of the reform, that is, to shape Italian arbitral legislation in light of foreign legal systems[56].

Secondly, the first sentence of the new provision also provides that the parties may only designate "provisions or a foreign law" as the law applicable to the merits[57]. Through this provision, the legislature eliminated the possibility for parties to choose Italian law as the law applicable to the merits of the dispute. Even this type of limitation on party autonomy is not in line with similar arbitration-specific choice of law rules, which do not provide such limitation[58]. Indeed, in almost all arbitration-specific choice of law rules[59], the parties are free to choose any "law" (understood as an exhaustive national corpus of law), not subject to the same restrictions that apply under the conflict of law rules in litigation[60]. Surprisingly, the legislature instead decided to limit the range of laws that parties can designate by excluding the possibility for parties to have Italian law governing the dispute. This decision contrasts with the reform's goal of promoting Italian-seated arbitration. Eliminating the possibility to choose Italian law does not promote resort to Italian-seated arbitration, but rather pushes Italian companies, with the economic power to impose a choice of law, to avoid Italian-seated arbitration. In fact, if these companies want Italian law to apply to the merits of a dispute, they will be prompted, because of this provision, to turn to other arbitral seats with greater autonomy.

6. The uncertainties generated and unresolved by the new provision

The new provision generates uncertainties that the legislature could have avoided. The employed formulation, "provisions or a foreign law", does not expressly clarify whether parties are allowed to also choose non-State rules to govern the merit of the dispute. As pointed out above, the most recent arbitration-specific conflict of law rules allows parties to designate "rules of law" to govern the merits of the dispute[61]. Unfortunately, the new Italian arbitration-specific choice of law rule is ambiguous on this point and does not

bring definitive certainty as to whether the parties are allowed to make such rules applicable. However, it should be noted that in the Explanatory Report to Legislative Decree nº 149/2022, the legislature refers to "*lex mercatoria*, UNCITRAL Model Law, and others," in relation to "the type of sources that can be invoked by the parties"[62]. However, if the provision were to be interpreted in the sense of allowing the choice of non-State rules, the legislature would have avoided all uncertainties by drafting the choice of law rule differently.

In addition, the text of the new provision fails to answer a number of questions. First, the provision does not clarify whether the choice of "foreign law" (*i.e.*, an exhaustive national corpus of law) is limited only to the substantive law of that State[63]. Moreover, the provision does not establish whether parties are also allowed to make an implicit choice of law or whether the choice must be explicit[64]. Further, the provision neither determines whether parties have the faculty of choosing more than one law applicable to the substance of the dispute[65], nor does it clarify whether and to what extent a negative choice of law is permissible[66]. Finally, the new paragraph of Article 822 does not elucidate which law should govern the validity of the choice of law.

In light of the critique above, the legislature could have better grasped the opportunity to reform (once and for all) a specific-arbitration choice of law rule resolving these issues.

7. Conclusion

To summarize, the new Article 822(2) CCP designed by the legislature is, for all the reasons stated above, not in line with the reform's goal of making Italy a more suitable arbitral seat and is not consistent with modern approaches to the parties' choice of law applicable to the merits. Indeed, the formulation employed by the legislature, in addition to leaving open a number of uncertainties, limits the autonomy of the parties temporally and substantively (excluding the possibility to choose Italian substantive law to govern the merits of the dispute). As suggested by commentary[67], I believe that the legislature should have modelled the reform after the arbitration-specific choice of law rule contained in Article 834 CCP, repealed in 2006, instead of adopting the new provision as it stands today.

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[1] See C. T KOTUBY, A. POMARI, *Do the 2021 Reforms of the Italian Code of Civil Procedure Make Italy a Favorable Seat for International Arbitration?*, in Matthias Scherer (ed), ASA Bulletin, pp. 344 – 358 (2022).

[2] See Article 1511 of the French Code of Civil Procedure; Article 187 of the Swiss Private International Law Act; Section 1051 of the German Code of Civil Procedure; Section 46 of the English Arbitration Act; Article 34 of the Spanish Arbitration Act; Section 27a of the Swedish Arbitration Act, introduced in the 2019 revision of the Act.

[3] Note: in the paper, this expression is used interchangeably with "arbitration-specific choice of law rule".

[4] See *supra* note 2.

[5] See *supra* note 1.

[6] I. e. a neutral law. See. W. KÜHN, *Express and Implied Choice of the Substantive Law in the Practice of International Arbitration*, in Planning efficient arbitration proceedings/The Law Applicable in International Arbitration, p. 383 – 384 (1996).

[7] See i.e. Article 187(1) of the Swiss Private International Law Act: " *the arbitral tribunal shall decide the case according to the rules of law chosen by the parties*"; Article 21 of the ICC rules; Article 35(1) of the UNCITRAL Arbitration Rules; Article 35(1) of the PCA Arbitration rules.

[8] F. FERRARI, L. J. SILBERMAN, *Getting to the Law Applicable to the Merits in International Arbitration and the Consequences of Getting it Wrong*, in Ferrari and S. Kroll (EDS), Conflict of Laws in the International Arbitration, p. 383 (2011).

[9] Such as "UNIDROIT Principles of International Commercial Contracts".

[10] See *supra* note 8.

[11] F. FERRARI, *Dell'opportunità di una regola di conflitto per individuare le norme sostanziali applicabili negli arbitrati internazionali con sede in Italia: una proposta*, In Studium Iuris, Rivista per la formazione nelle professioni giuridica, rivista mensile n. 9/2021 (2021), p. 1025

[12] See *supra* note 1.

[13] Legislative Decree February 2, 2006 No. 49.

[14] See *supra* note 2.

[15] See *supra* note 13.

[16] D. BORGHESI, *La Legge applicabile al merito*, in M. Rubino-Sammartano, Arbitrato, Adr, Conciliazione, pp. 567 – 580 (2009).

[17] See *supra* note 11.

[18] Author's translation of Article 834 of the Italian Civil Procedure Code, repealed by the Legislative Decree n° 49/2006.

[19] Author's translation of Article 822 of the Italian Civil Procedure Code.

[20] See *supra* note 11.

[21] Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I).

[22] Article 3(1) Rome I Regulation.

[23] See. F. RAGNO, Article 3, para 20, in F. Ferrari, Concise Commentary on the Rome I Regulation, 2 ed. (2020).

[24] See *supra* note 11.

[25] I.e. UNIDROIT Principles of International Commercial Contracts.

[26] See *supra* note 11

[27] See *supra* note 11, F. RAGNO: "[*t*]*he parties – by opting for non-national rules – incorporate those rules into the contract as contractual terms and, thus, can derogate from just the non-mandatory rules of the otherwise applicable law*".

[28] See supra note 11; P.A. DE MIGUEL ASENSIO, *The Rome I and Rome II Regulations in International Commercial Arbitration,* in F. Ferrari*,* The Impact of EU Law on International Commercial Arbitration, p. 177 *et seq* (2017).; F. ROSENFELD, *The Rome Regulations in International Arbitration: The Road not Taken*, in F. Ferrari, The Impact of EU Law on International Commercial Arbitration, p. 245 *et seq* (2017).

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

[30] See *supra* note 11.

[31] See *supra* note 11.

[32] Law No. 206/2021, Article 15, November 26, 2021, ("Enabling Act").

[33] Author's translation from the Enabling Act November 26, 2021 No. 206.

[34] Author's translation of Article 1(1) Enabling Act November 26, 2021 No. 206.

[35] "Piano Nazionale di Ripresa e Resilienza" ("PNRR") is the Recovery and Resilience Plan presented by the Italian Government to access the "Next Generation Eu" funds.

[36] Article 1(15) of the Enabling Act November 26, 2021 No. 206. See specifically paras. a-h.

[37] "Luiso Committee" (see *infra*) Explanatory Memorandum for the Reform of the Italian Civil Procedure, p. 17 (24 May 2021).

[38] "Luiso Committee" is the Commission for the Development of Interventions on Civil Process and Alternative Instruments (Pres. Prof Francesco Paolo LUISO), established within the Legislative Office of the Ministry of Justice in accordance with the Ministerial Decree of March 12, 2021.

[39] Author's translation of Explanatory Memorandum for the Reform of the Italian Civil Procedure, p. 17 (2021).

[40] *Ibidem*.

[41] See M. BENEDETTELLI, *Lett. D: Legge applicabile*, in Benedettelli, Briguglio, Carlevaris, Carosi, Marinucci, Panzarola, Salvaneschi, Sassani, L'arbitrato della legge di delega (commento ai principi in materia di arbitrato della legge di delega n. 206 del 21 novembre 2021, art. 1, c. 15), Rivista dell'Arbitrato, Fascicolo 1, p. 50 – 65 (2022).

[42] Author's translation of Explanatory Memorandum for the Reform of the Italian Civil Procedure, p. 17 (2021).

[43] See *supra* note 32.

[44] Author's translation of Article 1(15)(d) Enabling Act November 26, 2021 No. 206.

[45] See *supra* note 41.

[46] *Ibidem*.

[47] *Ibidem*.

[48] Particularly the gap relating to the identification of the criteria by which Arbitrators should determine the applicable law in the absence of a valid choice by the parties.

[49] Legislative Decree October 10, 2022, No. 149.

[50] Article 822(2) CCP introduced by the Legislative Decree October 10, 2022, No. 149.

[51] Author's translation of Article 822(2) CCP introduced by the Legislative Decree October 10, 2022, No. 149.

[52] Article 822(2) CCP.

[53] Explanatory Report to Legislative Decree October 10, 2022, No. 149 of October 19, 2022, Ministry of Justice (2022).

[54] See note 53, p. 99. Author's translation.

[55] For examples see *supra* note 2.

[56] See *supra* Section II, p. 3.

[57] See *supra* note 52.

[58] See *supra* note 55.

[59] I.e. Article 1511(1) of the French Code of Civil Procedure, "*the arbitral tribunal shall decide the dispute in accordance with the rules of law chosen by the parties or, where no such choice has been made, in accordance with the rules of law it considers appropriate*"; Section 27a of the Swedish Arbitration Act, introduced in the 2019 revision of the Act, "[*t]he dispute shall be determined by applying the law or rules agreed to by the parties*".

[60] See *supra* note 8, pp 373 – 374.

[61] See *supra* Section I, pp. 1 – 2.

[62] See *supra* note 53, p. 100. Author's translation.

[63] Namely whether the "renvoi" is prohibited or not, see *supra* note 8, p. 391

[64] See supra note 8, pp. 388-389.

[65] I.e. "dépeçage" see *supra* 8, p. 387.

[66] I.e., in contrast with a positive choice of law.

[67] See *supra* note 11.