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When Contractual Good Faith Meets a Controversial M&A Issue: The Sandbagging Practice in International Arbitration

Maxime Panhard*

I. Introduction

International Commercial Arbitration (ICA) is a forum where different legal systems meet, merge, and create autonomous rules, mostly unwritten and sometimes subjective. Given this autonomy, one interesting way to study the ICA approach to certain issues is to start with comparative law and add specificities of this system. The results give insights about what can be expected in ICA, as well as an illustration of the specificities of this system.

This article analyzes a mergers and acquisitions (M&A) issue known as the sandbagging practice. Sandbagging occurs when the buyer of a company brings a claim against the seller after the deal has closed for a breach of representation that the buyer knew about before the closing.¹ This issue occurs in civil and common law systems, but is approached with different legal grounds, including the contractual good faith principle. Despite this, ICA is the most used dispute resolution method with regard to transnational M&A disputes, and implies a very specific role for the contractual good faith principle.² Given the different national system solutions to the contractual good faith principle, it must be determined whether the frequent use of the good faith principle by international arbitrators can also be used to solve sandbagging practice cases in ICA.

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² See Beata Gessel-Kalinowska vel Kalisz, Representations and Warranties in Cross Border Mergers and Acquisitions: The Challenges of Cultural Diversity, 24 ICC International Court of Arbitration Bulletin 1, 32 (2013) (“The vast majority of disputes arising out of M&A transactions are resolved outside State courts. Arbitration is favoured [sic] by parties looking for expediency, confidentiality, a good understanding of business needs in M&A transactions on the part of the tribunal, and a spirit of cooperation that at best could lead to a settlement and will otherwise result in a fair and equitable award under applicable law.”); Ronald L. Hicks, Jr. & Amanda R. Gerstnecker, Litigation Issues in Asset Purchase Agreements, Ass’n of Corp. Couns., Dec. 1, 2011.
As this issue is controversial in different legal systems and international arbitrators widely use the good faith principle because of its subjectivity, sandbagging practice cases might be solved in ICA with the application of the good faith principle, balanced by the binding force of contracts.

A. The Sandbagging Practice: A Controversial Issue

Given the definition of the sandbagging practice, some practical reasons made it a controversial issue, which remains sensitive in different legal systems.

1. Definition of the Sandbagging Practice

The common definition of sandbagging usually refers to the idea of unfair treatment and misrepresentation. Indeed, this expression comes from the nineteenth century when robbers used sandbags to knock their victims out in order to rob them. Since the 1940’s, this expression is used in poker when a player acts like he does not have a good hand, when he actually does, in order to take advantage of his co-players. In golf, sandbagging occurs when a player pretends he is bad when in actuality he is good in order to gain handicap strokes and increase his chances of winning. In procedural law, the act of sandbagging has different meanings. It can be the act of voluntarily delaying a procedure, “in order to gain some benefit from the delay or prejudice to one’s opponent.” It can also mean voluntarily remaining silent when there is an error at a trial, with the idea of using the error for appeal if the decision does not meet a party’s expectations. Additionally, it defines the actions of a company facing a hostile takeover.


9. Id.

when it pretends to be negotiating for the sole purpose of gaining time to secure a more favorable offer.11

This article focuses on another definition of sandbagging, regarding the negotiation and execution of the representation and warranty provisions that are included in almost all private M&A negotiations.12 In the representation provisions, the seller communicates to the buyer all information that he knows, or that he is supposed to know, about the target company.13 These provisions allow both parties to determine the risks of the operation.14 After closing, in the event of a breach of the representation and warranty provisions, the buyer can bring an indemnity claim.15 In the latter situation, the sandbagging practice occurs when the buyer closes a deal despite knowing that the seller made a false or inaccurate representation, and then brings a breach of representation claim.16 The buyer performs due diligence prior to closing and might sometimes be a former executive officer of the company.17 If the buyer brings an indemnity claim after closing but had previous knowledge of the errors of the buyer, we are faced with what can be called the sandbagging practice.18

2. The Causes of the Controversy

Several practical reasons explain why this issue is so controversial, and can be found by studying the buyer’s perspective, as well as the seller’s perspective, given the contractual solution is not widely used.

da. Issues from a Buyer’s Perspective

Naturally, buyers tend to be pro-sandbagging.19 Indeed, from the buyer’s perspective, an important concern emerges parallel to extensive due diligence: if the sandbagging practice is not allowed, the buyer will claim that the more he knows about the company, the more his warranty will be inefficient.20 Practitioners’ common parlance for this is: “silence may not be golden,”21 “knowledge is not necessarily power,”22 or “a little

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11. Id.
15. Id. at 320.
16. Id.
19. See id.
knowledge can be a dangerous thing.”23 In an anti-sandbagging approach, because of due diligence, many elements will remain out of the warranty as the buyer is supposed to know of the breaches represented.24 Due diligence conducted prior to closing is so thorough that it could be claimed by the seller that the buyer is supposed to know almost everything.25 In an anti-sandbagging context, this serves to undermine the representations and warranties.26 Such a consequence would be unfair for the buyer, especially because knowing the existence of some misrepresentations does not necessarily include the knowledge of their impact.27

Permitting the sandbagging practice allows the buyer to isolate a risk without jeopardizing the entire operation.28 Thus, if a buyer discovers some elements that will constitute a breach of representations from the seller but doesn’t know yet the potential impact, he can still claim afterward a compensation based only on the consequences of this misrepresentation. This compensation is seen as a correction of the price initially paid.

Also, buyers frequently argue that they bought a so-called sandbagging-right with the price of the acquisition.29 The sandbagging-right means the buyers paid for a right to rely on the information disclosed by the sellers; thus, they are able to bring an indemnity claim in case of false information.30 This right exists regardless of their own previous knowledge.31 This idea implies a specific definition to the due diligence, as in such cases these are not only used for taking the decision to buy and at what price, but also to determine if there exists some breaches that will allow a post-closing indemnity claim.32

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28. West & Shah, supra note 6, at 3: “Rather than being forced to choose between negotiating a price concession or terminating or attempting to terminate the deal in such circumstances, the buyer may simply wish to enforce the benefit of the bargain it made by choosing to close the transaction and seek indemnification based upon the specific, contractual representations and warranties it negotiated with the seller.”
29. See Iovine, supra note 18.
30. Id.
31. Id.
32. Id.
Another issue frequently raised in favor of the buyer is that the knowledge of the breach can occur between signing and closing, without letting buyers cancel the closing. In such anti-sandbagging situations, the seller may organize the discovering of the breach by the buyer before the closing, but too late to avoid it, so the buyer won't be able to use this breach for a legal demand.33

b. Issues from a Seller’s Perspective

Naturally, sellers tend to be anti-sandbagging. Indeed, sellers argue that in a pro-sandbagging context, all the due diligence made prior to the closing has the sole objective of finding elements that constitute a breach of seller’s representations.34 These elements would then be used as a basis for a lawsuit after the closing. Sellers see this practice as particularly unfair, as the buyer knew of the breaches and could have taken them into account while negotiating the deal. As a consequence, in a pro-sandbagging context, sellers believe the extensive due diligence of the buyers’ counsel is intrusive and unfair, as the purpose can be to find breaches in the dispositions in order to file a post-closing claim.35

Sellers will also argue the sandbagging practice is a denaturalization of the purpose of due diligence. The original idea of this phase is to inform the buyer of the current situation of the company.36 In this idea, a seller allows a potential buyer to engage in due diligence to determine if they are for such a transaction and at what price.37 If due diligence is used to find breaches in order to bring a post-closing indemnification claim, the seller will feel ripped off.

Sellers have become more sensitive about this issue as the buyer’s due diligence investigations grew more extensive over the years.38

3. “Pro” and “Anti” Sandbagging Provisions

A contractual solution exists by including provisions to solve this particular point.39 Sellers favor anti-sandbagging provisions stating that the buyer cannot raise any demand, based on a breach, that he knew of before the closing.40 Buyers favor pro-sandbagging provisions, also known as knowledge savings provisions, stating that any previous knowledge of the breach by the buyer does not constitute a waiver of any potential claim based on this breach.

33. Id.
34. Id.
35. Miziolek & Angelakos, supra note 7, at 31.
36. Definition and Purposes of Due Diligence—Buyer’s Due Diligence, 1 CORP. COUNS. GD. TO STRATEGIC ALLIANCES § 9:2, Westlaw (database updated Sept. 2016).
37. Id.
38. Maynard, supra note 14, at 399.
39. See West & Shah, supra note 6, at 5.
40. See id.
Despite their efficiency, these provisions are not widely used in M&A practice. In 2014, the latest data available, only 35 percent of the acquisitions surveyed in the United States included a pro-sandbagging provision, 9 percent included an anti-sandbagging provision, and 56 percent remained silent about this question. In 2004, the same study showed there were more sandbagging provisions in acquisitions, but 39 percent remained silent on this issue at that time. In Europe during 2014, 24 percent of the transactions remained silent, 47 percent included an anti-sandbagging provision, 8 percent included a representation stating the buyer didn’t have any knowledge of a breach by the seller, and only 22 percent included a pro-sandbagging clause. Thus, depending on the regional business culture, the percentage of inclusion of a pro or anti sandbagging provision in the acquisition process varies. Nonetheless, this leaves plenty of room for operations that remain silent on this issue.

The context of the negotiations prior to closing explains why so many acquisitions remain silent on the sandbagging issue. If the buyer raises the inclusion of a pro-sandbagging practice clause in the purchase and sale agreement, the seller will suspect the buyer discovered some misrepresentation. If the seller has such doubt, he will certainly not accept any pro-sandbagging provision, but rather try to include an anti-sandbagging provision to avoid any risk. In consequence, talking about a pro-sandbagging provision for the buyer might lead to the opposite effect of what he was looking for. Eventually, most of the parties will find it safer to remain silent on this issue, giving room for the application of the default state rule.


Given these perspectives, the sandbagging act of the buyer is a very common issue in practice, regardless of the legal system. Taking the example of state courts in the United States (common law) and French courts (civil law), different grounds are used depending on the system, but

41. See id.
43. Id.
44. Id.
46. Leclercq, supra note 24.
the same issue remains. The French courts have an evolving approach, but must balance the contractual good faith and the binding force of contract.\textsuperscript{48} State courts in the United States diverge in their approaches, considering the indemnity claim either on a contract or tort basis.\textsuperscript{49}

a. French Courts: Balance Between Contractual Good Faith and Binding Force of Contracts

Despite an evolution in favor of the sandbagging practice in 2007, French jurisprudence compels practitioners to be very careful. Indeed, the sandbagging behavior of a buyer is mostly seen as contractual bad faith, even if the binding force of the contract usually prevails.

The French Civil Code provides, as in the majority of civil law systems, a very widely interpreted principle of contractual good faith. At the beginning of the nineteenth century, the first version of the French Civil Code, the Napoleonic Code, include article 1134 al. 3, dedicated to the principle of \textit{bonne foi}—good faith—in contract.\textsuperscript{50} This article remained unchanged in the French Civil Code until October 2016 when it was replaced by article 1104.\textsuperscript{51} This principle is interpreted broadly, including pre-contractual good faith,\textsuperscript{52} which commands the parties to be loyal in the negotiation and execution of the contract. This interpretation is broader than good faith applied solely to the execution of the contract. Therefore, in a civil law system, sandbagging practices can be challenged based on the good faith principle.

The jurisprudence of the \textit{Cour de Cassation}, France's highest civil court, on sandbagging related issues is often hard to interpret.\textsuperscript{53} For instance, the \textit{Cour de Cassation} confirmed the decision of the Court of Appeal, applying the principle of good faith in the contract to avoid the sandbagging practice.\textsuperscript{54} Yet, the very same court in a different case made a very strict application of the binding force of the warranty and allowed sandbagging.\textsuperscript{55}

\begin{footnotesize}
\begin{enumerate}
\item\textsuperscript{49} See West & Shah, supra note 6, at 3.
\item\textsuperscript{50} Code Civil [C. civ.] [Civil Code] art. 1134 (Fr.) ("Les conventions légalement formées tiennent lieu de loi à ceux qui les ont faites. Elles ne peuvent être révoquées que de leur consentement mutuel, ou pour les causes que la loi autorise. Elles doivent être exécutées de bonne foi") ("Agreements lawfully entered into take the place of the law for those who have made them. They may be revoked only by [their] mutual consent, or for causes authorized by law. They must be performed in good faith.").
\item\textsuperscript{51} Code Civil [C. civ.] [Civil Code] art. 1104 (Fr.) ("Les contrats doivent être négociés, formés et exécutés de bonne foi. Cette disposition est d'ordre public") ("Contracts must be negotiated, trained and executed in good faith. This provision is of public order.").
\item\textsuperscript{52} Philippe le Tourneau & Matthieu Poumarède, \textit{Bonne foi [Good Faith]}, \textit{Repertoire de droit civil [Directory of Civil Law]} (2017) n. 27.
\item\textsuperscript{53} Couret & Rosenpick, supra note 27.
\item\textsuperscript{54} Cour de cassation [Cass.] [supreme court for judicial matters] 2e civ., Oct. 11, 2005, Bull. civ. IV, No. 03-11390 (Fr.).
\item\textsuperscript{55} See generally Cour de cassation [Cass.] [supreme court for judicial matters] 2e civ., Oct. 11, 2005, Bull. civ. IV, No. 95-15191 (Fr.).
\end{enumerate}
\end{footnotesize}
In 2007, the Cour de Cassation eventually ruled that the binding force of contracts prevailed over the principle of good faith in regard to sandbagging practice:

If the rule according to which conventions must be performed in good faith allows the judge to condemn the unfair use of a contractual right, this doesn’t allow him to affect the substance of the rights and obligations legally agreed between the parties.\(^{56}\)

In this decision, the Cour de Cassation put in place a hierarchy between the principle of good faith and the binding force of contract, in favor of the latter.\(^{57}\) It is important to note the question of whether the buyer acted in good or bad faith does not belong to the Cour de Cassation, who only rules on the application of the law without qualification of the facts.\(^{58}\) In consequence, the Cour de Cassation cannot hold the sandbagging practice was performed in good or bad faith, but can rule on the hierarchy between binding force of contract and contractual good faith, two principles that are opposed in the sandbagging cases.\(^{59}\) The fact that contractual good faith finally appeared less relevant than the binding force of contract in sandbagging cases creates a hierarchy of those principles. Consequently, the sandbagging practice is allowed because of the prevalence of the binding force of contracts over the good faith principle even when seen as unfair by the courts.

Although some other decisions followed the 2007 decision, the uncertainty remained due to the fact that these were factual cases and the traditional preponderance of the good faith principle.\(^{60}\) Some authors recommended potential solutions, such as using the good faith principle to make a difference between knowledge of the breach and knowledge of the impact of the breach,\(^{61}\) or between knowledge of the breach and knowledge of the scope of the breach.\(^{62}\) The courts have not yet used these solutions,

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56. Cour de cassation [Cass.] [supreme court for judicial matters] 2e civ., Jul. 10, 2007, Bull. civ. IV, No. 06-14768 (Fr.) ("[S]i la règle selon laquelle les conventions doivent être exécutées de bonne foi permet au juge de sanctionner l’usage déloyal d’une prérogative contractuelle, elle ne l’autorise pas à porter atteinte à la substance même des droits et obligations légalement convenus entre les parties") ("[I]f the rule that agreements are to be executed in good faith permits the judge to sanction the unfair use of a contractual prerogative, it does not authorize it to infringe the rights and duties legally agreed between the parties.").

57. Xavier Delpech, Le devoir de bonne foi n’écarte pas la force obligatoire du contrat [The duty of good faith does not preclude the binding force of the contract], 2007 D. A. J. 2839.


59. Id.


61. Leclercq, supra note 24, at 179.

62. Courret, & Rosenpick, supra note 27.
and extreme caution remains, leading practitioners to be careful with this issue.\textsuperscript{63}

b. U.S. State Courts: On What Should the Buyer Have Relied?

Even if the U.S. legal system also integrated a contractual good faith principle,\textsuperscript{64} the issue of the sandbagging buyer depends on other legal grounds.

The historical law of warranty in the United States was mainly in tort, and evolved into a specific legal framework that some authors qualify as a: "curious hybrid, born of the illicit intercourse of tort and contract."\textsuperscript{65} Given these tort grounds, the courts used to consider that the representations in M&A operations were not part of the contract, so the demands based on their breaches were actions in tort.\textsuperscript{66} Thus, the sandbagging practice was rejected by the U.S. state courts because of the principle of reliance in tort actions. In accordance with that principle, the buyer is supposed to have relied on his own investigations—those that led him to the knowledge of the breach—rather than the warranty of the seller.\textsuperscript{67} If the buyer investigates and knows some representations are not correct, he cannot rely on them, but he must rely on his own investigation and thus, cannot claim any indemnity afterwards on the basis of the warranty. In that sense, the buyer waives any potential claim by closing the deal with the knowledge of the breach.\textsuperscript{68} Despite the fact the representations are included in the contract, many courts still rely upon a tort approach.\textsuperscript{69} This leads to discrepancies on the question of the necessity of reliance for a demand based on the breach of a contractual warranty or representation.\textsuperscript{70}

In some states, such as Delaware, a modern rule emerged based on a contract law approach.\textsuperscript{71} In this approach, the buyer doesn't only buy the company, but also buys the warranty. The price paid by the buyer includes "the cost of a sandbagging right."\textsuperscript{72} Naturally, this approach leads to pro-sandbagging decisions.

To understand these discrepancies, we can differentiate two types of reliance: the reliance in the traditional rule that implies the reliance of the buyer on its own investigation, in a tort action; and the reliance in the modern rule that implies the reliance of the buyer on the warranty he

\textsuperscript{63} Pierre-Menno de Girard & Charles-Audouin Pascaud, Garanties de passif: "1134, alinée 1er" contre "1134, alinée 3": combat de titans ou subtile alliance?, 2009 D. A. J. 2233-37.

\textsuperscript{64} RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981); U.C.C. § 2-103.

\textsuperscript{65} WILLIAM L. PROSSER, HANDBOOK OF THE LAW OF TORTS 651 (3d ed. 1964).

\textsuperscript{66} West & Shah, supra note 26, at 4.

\textsuperscript{67} See e.g., Assocs. of San Lazaro v. San Lazaro Park Properties, 864 P.2d 111, 115 (Colo. 1993).

\textsuperscript{68} Whitehead, supra note 1, at 1084.

\textsuperscript{69} West & Shah, supra note 6, at 5.

\textsuperscript{70} Id. at 4-5.

\textsuperscript{71} Whitehead, supra note 1, at 1081.

\textsuperscript{72} Id. at 1085.
purchased, in a contract-based action.\textsuperscript{73} In other words, the "buyer's reliance on the truthfulness of a seller's warranty," versus the "reliance on a promise necessary for the formation of a warranty."\textsuperscript{74}

It is important to note that the majority of the M&A transactions in the United States elect New York and Delaware laws.\textsuperscript{75} Even though Delaware courts have a clear pro-sandbagging approach, New York courts have a more complex system, adopting a contractual approach that does not necessarily lead to pro-sandbagging solutions. In \textit{CBS Inc. v. Zif Davis Publishing Co.}, the court adopted a contract approach and accepted the sandbagging practice, but only because the deal was closed, and the court made clear the buyer did not waive its claim regarding the specific breach.\textsuperscript{76} The reason for this is because the buyer mentioned the breach to the seller before closing the deal, but the buyer denied it.\textsuperscript{77} In subsequent cases based on New York law, such as \textit{Galli v. Metz}, the court rejected sandbagging practices even while adopting a contractual approach:

Where a buyer closes on a contract in the full knowledge and acceptance of facts disclosed by the seller which would constitute a breach of warranty under the terms of the contract, the buyer should be foreclosed from later asserting the breach. In that situation, unless the buyer expressly preserves his rights under the warranties (as \textit{CBS} did in \textit{Ziff-Davis}), we think the buyer has waived the breach.\textsuperscript{78}

Thus, the court considered that the buyer waived its claim when he had knowledge of the breach before closing.\textsuperscript{79}

In other decisions, courts applying New York law considered questions such as the origin of the knowledge of the buyer and the effects of the common knowledge.\textsuperscript{80} Eventually, if the knowledge of the breach comes from an explicit disclosure of the seller, the buyer has waived its claim.\textsuperscript{81} The New York case law, thus, implies a specific system in that the origin of
the buyer's knowledge, as well as the communication of such knowledge to the seller, play a major role.82

Courts are divided on this controversial issue, between states that adopt the modern rule, and states that apply the traditional rule.83 Furthermore, the reasoning and law principles that lead a specific jurisdiction to accept sandbagging are not always the same.84 Some states, such as Delaware, adopt a contractual approach that leads to pro-sandbagging solutions, but New York adopts a contractual approach that does not automatically lead to pro-sandbagging decisions.85 In consequence, the sandbagging judgment by the courts are not easily predictable in function of the state default rule.86 The decision will depend on the jurisdictions that have had the opportunity to consider this issue.87 These discrepancies reflect the controversial aspect of this issue. Accordingly, practitioners should remain cautious.

II. The Particularity of the Good Faith Principle in ICA

In M&A, representation and warranty provisions typically include an arbitration clause. This makes ICA the preferred dispute resolution method.88 Yet, precedents of national courts are not binding for international arbitrators, they massively use the contractual good faith principle, which has a different meaning for international arbitration cases as if it was used before national courts.

A. STARE DECISS FROM NATIONAL COURTS AND ICA

Judges from different legal systems apply different legal grounds, such as the good faith principle, to sandbagging practice cases. The question left to determine is whether, in a case of the application of a national law that includes the principle of good faith, but whose national courts never used it in the appreciation of the sandbagging practice, the international arbitrators may use it or not. In more generic terms, this is the common question of "whether [the arbitrators] should follow the case law of domestic courts of the jurisdiction whose law applies to the contract before them."89 We are not talking about the common debate of binding precedent between arbitral

82. Id.
83. Whitehead, supra note 1, at 1084-85.
84. Miziolek & Angelakos, supra note 7, at 31-34.
85. Id.
86. Iovine, supra note 18, at 10 ("Even though this so-called 'pro-sandbagging' default rule in Delaware and New York may mean that a majority of buyers will have some right to sandbag, even if an acquisition agreement is silent on the issue, buyers should be aware that sandbagging case law has only recently started to evolve and these default rules continue to have some ambiguities.").
87. Duchemin, supra note 72, at 689.
88. Gessel Kalinowska vel Kalisz, supra note 2, at 32.
awards. Instead, we are talking about determining whether international arbitrators should take into account the case law of the national courts applying the applicable law.

The role of precedents is one of the main differences between the construction and use of the two legal systems studied here: common law and civil law. If common law incorporates a strong binding precedent principle that applies to its courts, civil law countries usually do not include such principle.90 In civil law countries, precedents from higher courts usually play an important role in the interpretation of the law because lower courts try to respect such interpretation in order to avoid having decisions undermined.91 However, international arbitral tribunals are created on a case-by-case basis, and produce only one award regarding the case for which they are created.92 They do not have any previous decisions and thus, cannot have any concern regarding the inconsistency or consistency of their award with their previous one.93 Additionally, the award taken by an international arbitral tribunal is not supposed to be subject to review by national courts.94 In consequence, such tribunals should not be concerned, as domestic judges are, by the risk of having their award reversed by a higher court.95 Furthermore, the awards remain generally confidential and unpublished in such a way that should prevent the creation of any case law in ICA.96 Finally, one of the reasons for choosing ICA to resolve disputes can be to have an application of the law adapted to fit the needs of international business—a feature that doesn't belong to the domestic courts—while also allowing the international arbitrators to disengage from national case law.97

In consequence, even if international arbitrators frequently used court precedents, like U.S. judges,98 case law is not binding, and the arbitrators are not compelled to follow domestic decisions if the situation requires a different solution.

B. THE SPECIFICITY OF THE CONTRACTUAL GOOD FAITH PRINCIPLE IN ICA

The principle of contractual good faith, that might apply to sandbagging cases, as shown by the precedent developments, is very specific in ICA. It

90. Id. at 250.
91. Id.
92. Id. at 253.
93. Id. at 252.
94. Id.
95. Id. ("[A]rbitrators—unlike judges—are appointed for the resolution of only a single dispute and issue final decisions that are not subject to appeal, i.e. a ‘révision au fond’ of their rulings by the competent domestic courts in setting aside proceedings at the seat of the arbitration is not permissible.").
96. Id. ("In addition, their awards are usually not published and they, therefore, need not and cannot be concerned with the consistency of their decisions with other awards.").
97. See id. at 252–57.
98. Id. at 252.
became a major concept of international law widely used by international arbitrators, and is very flexible when used in ICA.

1. **Contractual Good Faith: A Major Concept of International Law**

Due to the development of international treaties and international trade, the principle of contractual good faith is now recognized as a fundamental principle in international law.99 The Vienna Convention of the Law of Treaties introduced the general principle of good faith regarding performance of treaties in 1969.100 The United Nations Convention on Contracts for the International Sale of Goods included the contractual good faith principle in 1980.101 The International Court of Justice also referred to the contractual good faith in some of its decisions.102 Regarding international trade, contractual good faith was included in the UNIDROIT Principles in article 1.7, which provides:

Art. 1.7: (Good Faith and Fair Dealing)

(1) Each party must act in accordance with good faith and fair dealing in international trade.

(2) The parties may not exclude or limit this duty.103

This inclusion in the UNIDROIT Principles reflects unanimous recognition of contractual good faith at an international trade level.

2. **Contractual Good Faith: Widely Used by the International Arbitrators**

The wide use of the principle of good faith by international arbitrators is well-known.104 This principle is so frequently used in ICA that the parties cannot pretend to avoid it.105 International arbitrators refer to the good faith

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100. Vienna Convention on the Law of Treaties, art. 26, May 23, 1969, 1155 U.N.T.S. 331 (“Noting that the principles of free consent and of good faith and the pacta sunt servanda rule are universally recognized . . .”); see also Channel Tunnel Group Ltd. v. U.K., 2003-06 PCA Case Repository, Partial Award, 1, 25 (Perm. Ct. Arb. 2007) (noting that the parties agreed to use the Vienna Convention of the law of treaties as a guide to the interpretation of both the treaty and the international contract).
101. United Nations Convention on Contracts for the International Sale of Goods art. 7(1), 1980, 10 U.S.T. 56997 (“In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.”).
principle via the application of a national law or via the application of the principles of international law. They can also apply it despite the requirements of the applicable national law. UNIDROIT Principles are part of the lex mercatoria that is used as legal basis by international arbitrators, and as seen above, include a good faith principle. In fact, these principles usually imply material rules of the lex mercatoria, and the principle of good faith is the most used UNIDROIT principle to create some material rules. Indeed, as Pierre Mayer mentions, around half of the lex mercatoria principles pointed out by Lord Mustill can be directly linked to the principle of good faith. Therefore, the principle of good faith appears to be "the principle of the principles." In this sense, the principle of good faith serves as the basis for other rules and even other general principles, thus, becoming "one of the richest sources of lex mercatoria." Eventually, the good faith principle became a rule used as a basis for an international arbitration demand, starting with the Norsolor case.

3. Contractual Good Faith: A Flexible Principle When Used in ICA

The notion of good faith and its use as a principle can vary depending on the legal system where it is applied, and whether it is applied in either a national or international context. This is true even inside the same legal system.

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106. Mayer, supra note 104, at 548.
108. Karton, supra note 107, at 141 ("When transnational law is invoked, tribunals almost invariably point to a codified instrument, such as the UNIDROIT Principles, CISG, INCOTERMS, or UCP 600. Codified instruments appeal to international arbitrators because they represent an international consensus. More importantly, they are predictable, and therefore, palatable to commercial parties, which crave certainty.").
109. UNIDROIT Principles, supra note 103.
111. Mayer, supra note 104, at 554 ("[E]nviron la moitié des vingt principes de lex mercatoria cités par LORD MUSTILL dans son article aux Mélanges Wilberforce ont été expressément rattachés au principe supérieur de la bonne foi, qui apparaît ainsi comme le principe des principes.").
113. Cremades, supra note 99, at 783.
114. Pedro J. Martinez-Fraga, Good Faith, Bad Faith, But Not Losing Faith: A Commentary on the 2010 IBA Rules on the Taking of Evidence in International Arbitration, 43 Geo. J. Int'l L. 387, 412 (2012) ("At the very outset, the concept of good faith is contingent upon the legal tradition, culture, and system in which it appears. The challenge in interpreting the concept of good faith goes far beyond even the fundamental civil/common law divide because even within the
These changes are a consequence of the subjectivity of the good faith principle, which has to be interpreted in the context of the case. Indeed, the perception of good faith itself necessarily implies subjectivism, and therefore, uncertainty.\textsuperscript{115} Thus, at an international level—particularly in international commercial arbitration where each arbitral award is independent from the others excluding any doctrine of precedent or \textit{stare decisis}—the subjectivism of the good faith principle comes into play.\textsuperscript{116}

This subjectivism of the good faith principle is also an explanation of its success in ICA, and its worthwhile elasticity.\textsuperscript{117} Pierre Mayer explained the reasons for such usage that come from this subjectivism. According to him, the good faith principle is used by the arbitrators as a way for them to add equity in their decisions.\textsuperscript{118} Yet, only the subjectivity of this principle, especially when put in relation to the context of the case, allows arbitrators to add some equity in a law-based decision. Thus, arbitrators may use the good faith principle to adapt the application of the law to the equity required by the international practice, giving this principle a more dynamic role, "unknown (or unseen) in the law."\textsuperscript{119} Some awards have stated in this sense, using the principle of good faith to challenge the strict application of other legal rules.\textsuperscript{120}

The purpose of ICA in itself explains the use of a flexible good faith principle by international arbitrators. As already stated by Philippe Fouchard in 1965, the interest of international arbitration is to find satisfactory outcomes for international litigation cases according to rules that belong to international trade, and to apply rules that are more adapted than the national laws.\textsuperscript{121} Thus, ICA became the main way to determine and apply international business law, and one of its virtues is its capacity to provide laws adapted to fit the needs of international trade.\textsuperscript{122} Also, as framework of civil law jurisdictions, different meanings of good faith are recurring and readily discernible.

\textsuperscript{115} Jacques Flour et. al, \textit{Les obligations, 1. L’acte juridique}, 402 (Dalloz eds. 2014) ("La notion même de bonne foi est entachée d’une irreductible incertitude et d’un incompressible subjectivisme").


\textsuperscript{117} Ejan Mackaay et al., \textit{L’économie de la bonne foi contractuelle}, 422, 433 (2003) ("l’élasticité louable du principe") ["the laudable elasticity of the principle"].

\textsuperscript{118} Mayer, \textit{supra} note 104, at 543.

\textsuperscript{119} Id. “La seconde cause est propre à la place que tient la bonne foi dans la lex mercatoria. Celle ci ne se borne pas à recevoir en son sein les solutions consacrées par les droits étatiques; elle donne au principe de bonne foi un rôle plus dynamique, inconnu (ou invisible) dans le droit” [The second cause is peculiar to the place of good faith in the lex mercatoria. This is not limited to receiving within itself the solutions consecrated by state rights; it gives the principle of good faith a more dynamic role, unknown (or invisible) in law.].

\textsuperscript{120} See Award in ICC case no. 4761, Clunet 1012, 1015, 1017 (1987); ICC case no. 6129, 1047 (1990); Isabelle Barrière Brousse, \textit{Efficacité du contrat et arbitrage commercial international}, L’efficacité du contrat, Dalloz, 2011, at 84; Mayer, \textit{supra} note 104, at 543.

\textsuperscript{121} Philippe Fouchard, \textit{L’Arbitrage Commercial international} (Dalloz, 1965).

\textsuperscript{122} Eric Loquin, \textit{L’arbitrage du commerce international} (Joly eds. 2015).
briefly explained in the introduction, one of the main reasons for the choice of international arbitration as a litigation resolution is that it will usually reflect international practices. Indeed, the simple choice of international arbitration frequently implies the will of the parties to have a decision adapted to the current practices of the international trade. In a more general sense, international commercial arbitration prevents legal uncertainty in international operations. National rules do not always fit the needs of international transactions, so international arbitrators have elaborated transnational material rules, inspired by their national system, international conventions, or practices in international trade.\(^{123}\) To reach such adaptability, a flexible good faith principle is an efficient tool for international arbitrators.

### III. Consequences Regarding the Sandbagging Practice in ICA

Given the use and specificities of the good faith principle before international arbitrators, it is more likely to be applied to reject sandbagging practice in ICA; however, the *pacta sunt servanda* principle still remains a major basis of international trade. Finally, international practice and needs could involve less bad faith qualification for sandbagging buyers' acts.

#### A. Contractual Good Faith Used to Reject Sandbagging Cases in ICA

Given the uncertainty that remains regarding sandbagging practice in the national systems, international arbitrators can easily use the good faith principle to match the rule of law with the expected behavior, in good faith of the parties in sandbagging cases. This is more likely to occur when arbitrators think the behavior of the sandbagging buyer is unfair, and therefore, want to reject his claim. Indeed, they would prefer the binding force of contract—*pacta sunt servanda* principle—if they want to decide that a sandbagging claim is fair.

#### B. The Prevalence of the *Pacta Sunt Servanda* Principle

One of the most recognized principles in international contract law is the binding force of the contract—*pacta sunt servanda* principle. As already mentioned, the good faith principle is frequently linked to the *pacta sunt servanda* principle when highlighting their importance and unanimous recognition among the legal systems.\(^{124}\) In fact, the good faith principle is frequently perceived as linked to the *pacta sunt servanda* principle in order to determine what a party shall expect in the execution of the contract in good faith from the other party.\(^{125}\) We can note regarding international

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123. Barrière Brousse, *supra* note 120, at 84.
125. Id.
conventions, the good faith principle is inserted inside the article relating to the *pacta sunt servanda* principle in the Vienna Convention: "Every treaty in force is binding upon the parties to it and must be performed by them in good faith."  

The statements of the parties of this Convention, already mentioned, also link these two principles: "Noting that the principles of free consent and of good faith and the *pacta sunt servanda* rule are universally recognized."  

This principle is also present in the UNIDROIT Principles: "A contract validly entered into is binding upon the parties. It can only be modified or terminated in accordance with its terms or by agreement or as otherwise provided in these Principles."  

Thus, even when deciding that the behavior of the sandbagging buyer qualifies as contractual bad faith, arbitrators will always have to balance the good faith principle with the binding force of the contract. They might decide, in function of the cases, that the binding force of the contract prevails over the principle of good faith, as did the French *Cour de Cassation* in its 2007 decision.  

Not surprisingly, the available awards show that international arbitration usually favors the application of the contract, even if it is sometimes challenged by the good faith principle in order to maintain a certain balance between the obligations of the parties.  

C. Evolution of the Practice: Sandbagging Could Be More and More Good Faith  

In the ICA context, and today, the sandbagging behavior of a buyer will not necessarily be considered bad faith. Indeed, as stated above, a consequence of the subjective notion of good faith in ICA is to allow the international arbitrator the ability to adapt his decision to the international practice. Yet, some courts allow sandbagging because of the binding force of contracts (regardless of its good or bad faith qualification). Once legally admitted, this practice will be regarded as less and less unfair. In consequence, the application of the contractual good faith principle can also lead to pro-sandbagging repercussions in ICA, as the sandbagging action of the buyer might be seen as less and less unfair in practice.

IV. Conclusion  

Two main concluding observations can be inferred from the above. First, the wide use of the good faith principle by the international arbitrators, and its application regardless of the will of the parties or the applicable law, make
its consideration inevitable in a sandbagging practice case, especially given the controversial nature of this issue. Second, because of the evolution of the international practice and the *pacta sunt servanda* principle, the application of the good faith principle in ICA does not necessarily imply a sanction of the sandbagging practice. Still, practitioners should keep in mind that the consideration of the good faith principle might occur in sandbagging cases before international arbitrators, and should therefore take it into account in their strategy when counseling a client.133

133. Cremades, *supra* note 99, at 766 (“For those who set the parties’ strategy when a case arises in which good faith may play a material role, the major question to ask is whether or not the legal culture and training of the potential arbitrators might condition their ultimate decision. Counsel must be aware of the various angles that can be given to good faith in legal argument, as well as in the arbitrators’ decision-making process.”).