Kluwer Arbitration Blog

Some Cost Consensus?

Nicolas Ulmer (Budin & Associés Avocats) · Wednesday, May 4th, 2011

Throughout 2010 and into this year there have been numerous entries on this blog dealing with various aspects of international arbitration's lack of efficiency and runaway costs, and proposing various remedies or reforms. These have included contributions from Roger Alford, Lucy Reed, Niuscha Bassiri, Philipp Peters, Lisa Bench Nieuweld, and many provocative posts from Michael McIlwrath—I apologise if I have not listed all who posted material on this timely theme. This spring Arbitration International published my article "The Cost Conundrum", where I argued for reforms in the "arbitration industry", but also sought to explain that the rise in arbitral costs and procedural complexity has many sources and not one solution. Since then I have taken due note of Rusty Park's article "Arbitrators and Accuracy", 1 J. of International Dispute Settlement 25 (2010) which concludes: "Efficiency without accuracy will prove an empty prize." It is indeed true that few parties want efficiency at the cost of not having their case properly heard; the trick is to reform matters such that the admitted or agreed excesses of arbitration are reduced without sacrificing fair and accurate procedure; not easy, but not impossible. The cost debate in international arbitration has largely been provoked by in-house counsel complaints, yet Roger Alford's 8 July 2010 blog entry reports on a corporate counsel discussion that long-discussed these issues without reaching consensus as to the solutions.

I would like here discuss a few themes where there appears some evolving consensus—or at least I am fairly clear—as to appropriate reforms, and identify some of the key factors and players in carrying them out. The full solution, if any, to the distention and rising costs of arbitration may be long in coming, but this may be a start.

1. Arbitrator Availability and Attentiveness.

There have been numerous complaints in this blog and elsewhere concerning the unavailability of many arbitrators for hearings, their tolerance of excessive procedures, their failure to render awards within a reasonable amount of time and, more generally their lack of diligence and celerity. Many of these complaints are justified, and I share them. The way out is through the door—a point ably made in Lisa Bench Nieuweld's January 2011 blog entry ("Choosing the Weathered Veteran or the Young Buck?"). So long as Parties, usually on the recommendation of their outside counsel, wish to nominate overbooked "Gorrillas" (Jean-Claude Najar's term for the escalation to "big name" arbitrators) they will often suffer from this problem. It is not true that the less well-known arbitrator is necessarily the "chimpanzee" on the panel—to the contrary I have found that the effective arbitrator is the one who gives the case his or her best attention and the key arbitrator quality is hard work. Schedule distention and the unavailability of hearing dates are, of course,

compounded when one is dealing with a three-person tribunal, particularly three “Gorillas”. But many parties are reluctant to nominate a “young buck” as arbitrator, or to agree to a sole arbitrator once a dispute has arisen. Thus many contracts do not stipulate for a sole arbitrator, and often parties resort to the real of imagined security of nominating an arbitrator, and only agreeing to a chairman, that is an overbooked “known name”. I might add that in my three or four experiences where there was a three person tribunal entirely appointed by an arbitral institution a different, but more efficient, case dynamic imposed itself—this suggests that the presence of party-nominated arbitrators often has a negative impact on efficient procedure, although it cannot be quantified. If parties are prepared to opt for a sole arbitrator, or dispense with the perceived advantage of nominating “their” man (or woman) and an agreed chairman, they will likely gain in efficiency—but that is not always a choice they are always prepared to make.

The arbitrator(s) must not only be available, but also attentive, i.e. willing to put in time on the case from the beginning, and ask questions of the parties early, so that the case can be focused and the dispute potentially reduced or even resolved. There are numerous justified complaints of evidentiary and discovery excess in arbitration; not a few of them would be solved by greater early attentiveness by the arbitrator. It is not, for example, possible properly to rule on the true need and materiality of many document requests without having a strong understanding of the real issues in the case and what might or might not be necessary to plead and decide them fairly. Arbitrators who have not taken the time and effort (which may be substantial) early to study the case will not be in control of the discovery process or have a basis to limit it effectively. I would add that the problem may be compounded when the arbitrator does not regularly act as counsel, or hasn’t done so in many years: they don’t have an “insider” view of how cases are constructed or proof presented and, not infrequently, make rulings that betray this, and do little to promote efficiency. It is better to have an arbitrator with a personal knowledge not only of the genre of dispute at hand, but of the costs and efforts necessary—and unnecessary—to present it. This point ultimately devolves into to the “Gorilla” problem, and the increasingly controversial phenomenon of the “professional arbitrator” with a purpose-built “arbitration shop.”

The message appears to be out on this aspect of arbitral distention and its impact on costs. The ICC took up part of the point with their requirement of a Statement of Acceptance, Availabilty and Independence. Lucy Reed went further in her blog entries and proposed the “Reed Schedule” where arbitrators would prior schedule time to allow–or force—them to organise the procedure, prioritise issues and, presumably, deliberate. There have been a number of proposals for data banks that would tabulate arbitrator performance and timeliness. Greater transparency concerning arbitrator performance is necessary and, I believe, inevitable—so arbitral institutions, concerned parties and potential arbitrators should work to ensure that accurate and proper information about arbitrator performance becomes available. These seem radical proposals to some, but it is a new digitalised world, and reliance on perceived reputation and gossip about arbitrators has not sufficed to prevent nomination of arbitrators prone to delay, inattention and overbooking.

2. Counsel and Client

Michael McIlwrath has frequently blogged on these pages about how arbitration counsel, miss the point: companies such as GE are not wedded to arbitration, they are seeking to solve a dispute and limit its financial and commercial consequences. McIlwrath repeatedly advocates mediation, and bates arbitration counsel with his call for “anti-arbitration.” I gather GE practices what it preaches and there are indeed many disputes that can be solved—with less commercial fallout—through mediation. I had a good experience of this last year in Zurich where, after midnight on the second

day, we agreed on a number (only to then argue about the non-disclosure and non-disparagement clauses that we wanted.) Reflecting on this and a few other experiences I see several items that led to a successful resolution: the first, of course, was that the contract required prior mediation and both parties were amenable to it (and did not seek the opportunity to argue about some potential ambiguities and gaps that needed to be filled in the mediation procedure.) The second was good preparation on our side; I well knew the in-house counsel and we prepared effectively: he handled the technical issues (software licensing) and corporate communications and I handled the "legal" and "arbitration" issues (Swiss and Swiss). Reflecting on that experience I would say that the mediator's primary role devolved into convincing the other side that we had analysed the case and were serious in our belief that are our potential liability, should the matter not settle and be taken to arbitration, was not extensive i.e. that the other side had a tough case if they did not accept what was offered. We ultimately settled for an amount that my client had always been willing to pay to make the matter "go away." The key element in the mediation was, I believe, that the other side became convinced that they were not likely to do better in a subsequent arbitration. I might add that preparation for mediation was fairly costly, albeit a fraction of what an arbitration would have cost.

The problem is that mediation is not always possible, and for international contracts arbitration will always be a necessary tool, or a necessary evil. Many arbitrations arise from serious or complex issues and/or issues where it is difficult for one or both parties to agree to mediation: very often the parties are not of equal sophistication, and not infrequently one party is not entirely in good faith. Arbitrations between sophisticated parties who are continuing to do business together do arise, but is in my experience are not the norm, and for each such dispute that reaches arbitration there are probably a dozen that have been solved, through negotiation without even reaching mediation. But when such disputes do reach arbitration it is a common phenomenon that they escalate out of proportion and result in very significant legal fees.

None of this is to excuse runaway fees, and research shows that legal fees are the main driver of the higher arbitration costs that have become unacceptable to many in industry. McIlwrath's comment "…Feedback on Your Recent Pitch" (12 April 2011) was clever and sarcastic—and he is certainly right that these pitches all resemble each other—but it is not entirely fair to assign all the blame to counsel from large firms that so vigourously promote their arbitration department. These and other counsel will be responsive to early solutions, real efficiency and even the need for mediation if that is made clear to them—or if they know there is no alternative. In particular, good arbitration counsel welcomes the clear directions and deep involvement of in-house counsel who will have an industry and corporate understanding that can be key to the case. So the initial role in these reforms should probably come from sophisticated in-house counsel, the deciders for the "consumers" in the "arbitration industry."—and they appear to be taking this role on.

It is also the role of in-house counsel to ensure that dispute resolution clauses in the company's contracts keep up with and take advantage of what is offered by the market, not only a properly structured mediation procedure, but other potential dispute resolution efficiencies. For example there has been generally good experience with the Swiss Rules "Expedited Arbitration" (one arbitrator, six-month time limit, one round of briefing, accelerated hearing) and many other institutions are putting similar products on the market, e.g. the ICDR Protocol, which McIlwrath reproduces in one of his earlier blog entries. There is a ying to this yang, however: in-house counsel and their company have to be comfortable with the risks, as well as the cost advantages, that abbreviated procedures entail in practice. They then have to assume those risks without knowing the details of the dispute that could in the future be submitted to such procedures—but

this, as with the prior stipulation of a sole arbitrator, is a choice that can be made.

Finally, or almost finally, I have read the criticism that outside arbitration counsel do not do a sufficient up-front analysis of the damages that might be awarded in a potential arbitration—they wrongly leave this to a later stage. I suspect this is largely correct, and it is certainly not a minor point: You can have all the breaches of contract in the world, but if they do not translate into clear and provable damages there is little point in proceeding full-bore and the case can take on a life well beyond its true "value". Indeed, sitting as arbitrator I have often found that even at the end of the case there were aspects of the damage claims and calculations that were insufficiently pleaded or documented. Part of the problem is that most lawyers like arguing contract and liability issues, but damages are often difficult and tedious. But I have also, as counsel, found that many clients are reluctant to spend the up-front costs and time necessary to make a full case and damage assessment, in the hope that the case will settle, or the issue become clearer later when "we see what the other side answers". In fact, the chances of settlement and efficient procedure are often enhanced if the parties have a clear and confident analysis of what damages are likely, or unlikely, to be awarded. Here the fault must be shared between in-house and outside counsel.

At the end of the day there are techniques for controlling counsel costs—and they depend in large part on effective communication and teamwork between client and counsel, and in some cases tough decisions by the former. This is particularly true in the small and medium sized arbitrations (a few million dollars) which still predominate although they don't get the star billing. One technique on such cases is to have an agreed monthly bill and budget, time-limited and augmented, or diminished, should the case take an unexpected turn or change in timing. This can work well if properly and cooperatively thought out: the client knows and can project what is being paid and outside counsel knows the budget he must work within. If this be the "commoditisation" of arbitral work then so be it. You still cannot control what the other side is serving up—but if in-house counsel does not care for the standard menu of hourly rates (however "competitive") he or she must order a meal to fit the occasion (and only tip for good service.).

3.Costing Costs

"The instant Cost Order" proposal advanced by Nuischa Bassiri on this blog (10 October 2010) is an attractive idea whose time may have come. All too often there are unnecessary applications, disclosure requests or plain violations of the rules in arbitration proceedings. One of the few sanctions arbitrators have is costs. It is likely that counsel—or at least his or her client–faced with the prospect of not only paying for a dubious application, but also paying the other parties reasonable costs in opposing it would desist from far-flung motions. Were a motion found to be excessive and unjustified the arbitrators would indicate that costs in a specified amount would be awarded to the other party, and this would be reflected in the final Award—either directly or by deduction from the costs allowed the party who made the improper motion. I do have three cautions about this proposal: First, it is a deviation from the largely followed rule that costs follow the (substantive) event—this would introduce the concept of running procedural costs, unrelated to whether the party running up these costs prevailed on the merits. The second point is that of unintended consequences: such a reform would necessarily give the parties something more to argue about—whether the failed action or motion was sufficiently unmeritorious as to justify the sanction of costs and in what amount? Finally, the success of such a development would necessarily depend on attentive and firm arbitrators prepared to "police" the procedural case in this way—which gets us back to point one, above. In my view such a reform would best be inserted in the applicable rules for the arbitration so as to give the arbitrators more basis and backbone in

awarding procedure-related costs during the proceeding. In my experience arbitrators are very reluctant to do so and just defer the request for such costs to the final Award, where it gets lost in the wash.

The English litigation concept of “sealed offer” costs (i.e., if the award is for less than the losing party offered in settlement then the costs are taxed against the party that refused such offer) has been advanced as a desirable reform for international arbitration. It is a logical concept for encouraging settlement and apportioning costs but it is not logistically feasible in most international arbitrations, as it implies or requires a separate cost hearing after the substantive Award has been rendered, a procedure only justified in a few, very large, cases.

But attentive arbitrators prepared to make use of a power of “instant” cost awards during the procedure would likely diminish cost and abuse, and it would be salutary if arbitrators would use cost allocation more directly to sanction parties for procedural error and abuse. But this will only have a minor, if positive, effect in diminishing the arbitration costs and delay that is complained of—and is far less important that the reforms discussed in the first point above.

There is much more that can be said, and done, to try to reform some of the excesses of arbitration and their cost impact; I have only blogged on a few points. It should be recognised that each procedural “solution” will necessarily involve a trade-off of some kind—but that is not an excuse for seeking and implementing better and more cost-effective practices.

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