Arbitral, Not Arbitrary – Part I: Limits to Arbitral Discretion in ICSID Arbitration

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The problem of arbitral discretion has major implications on the rights of the parties. It is a concept foundational to international arbitration. Yet, it has proven to be so elusive as to escape any definition or treatment in literature.

Why is this topic important?

In order to answer this question, let us take pre-award interest as an example. The *Wena v. Egypt* ad hoc committee has prominently held that "international tribunals… dispose of a large margin of discretion when fixing interest." (ICSID Case no. ARB/98/4, Decision on annulment of February 5, 2000, para. 96) Pre-award interest is part of the compensation for the damage resulting from the fact that the creditor is deprived of the use of the sum he was supposed to receive. (*Vivendi v. Argentina*, ICSID Case no. ARB/97/3, Award of August 20, 2007, para. 9.2.3.) In cases such as *Compañía del Desarrollo de Santa Elena, S.A. v. Costa Rica* where the breach occurred – and consequently the *dies a quo* was – 20 years before the date of the award the interest on the outstanding principal would exceed it several times. Thus, the Santa Elena tribunal awarded more than U.S.$ 11 million in interest on a claim of over U.S.$ 4 million. (ICSID Case no. ARB/96/1, Final award of February 17, 2000, para. 95) In this regard, a passage appearing in *SGS Société Générale de Surveillance S.A. v. Philippines* Order on further proceedings seems particularly troubling. There the tribunal noted *in passim* that:

> "[C]ounsel for the Claimant formally abandoned its claim for contractual interest… Instead, he asserted **a claim for interest at international law**, i.e. extra-contractual interest. **But whereas international tribunals do have the power to award interest on unpaid amounts, that is a discretionary power** and depends on the circumstances. Guidance may be obtained from the decision of the Permanent Court of International Justice [in the Wimbledon case] where interest was awarded **only from the date of judgment**, that being 'the moment when the amount of the sum due has been fixed and the obligation to pay has been established'." (ICSID Case no. ARB/02/6, Order on further proceedings December 17, 2007, para. 16; emphasis added)

While determination of the applicable rate of interest deserves further research in its own name and may depend on the applicable law, nature of the breach of obligations, nature of the investment etc., the position of the tribunal is striking as one making a reversal to the state of the law back in the year 1923. The *Wimbledon case* (*Case of the S.S. "Wimbledon"*, Judgment, Permanent Court of

International Justice Series A No. 01 (1923)) belongs to an time when interest was consistently denied for the so-called unliquidated claims (that is, claims in which the exact amount of the loss is fixed by the award itself) and does not any more reflect the current state of the law. (*Second report on State responsibility*, Special Rapporteur G. Arangio-Ruiz in Ybk ILC 1989 vol. II at p. 27) Consequently, it may be agreed that determination of the rate of interest falls within the discretion of the tribunal, however, it must be recognized that the claimant is entitled to pre-award interest as of right, i.e. in any case in which valuation is effected as of date preceding the award – most often the date of the breach, (See for e.g. *Asian Agricultural Products Limited v. Sri Lanka*, ICSID Case no. ARB/87/3, Award of 27 June 1990, para. 114; *Southern Pacific Properties (Middle East) Limited v. Egypt*, ICSID Case no. ARB/84/3, Award of May 20, 1992, para. 234) and should not depend on the discretion of the tribunal alone. Otherwise, the functions of pre-award interest will be hindered, namely, timely settlement of the dispute; reinstatement of the creditor in the position before the breach and denial of unjust enrichment of the respondent, especially with a view to the fact that during this time the latter has been able to earn interest on the withheld amounts.

Characteristics of arbitral discretion and a possible definition of the concept

The rationale behind the concept of arbitral discretion is effective case management. In addition to that, the arbitration rules cannot beforehand and in detail provide for every possible situation occurring in a dispute.

To give an example, consider the situation which presented itself in the *Himpurna California Energy Ltd. v. Indonesia* arbitration in which agents of the Republic of Indonesia intercepted Professor Priyatna Abdurrasyid, one of the co-arbitrators, at Schiphol Airport in Amsterdam in order to prevent him from further participating in the proceedings. The other two arbitrators had to interpret the provisions of the UNCITRAL Arbitration Rules and reached the conclusion that a truncated tribunal can proceed to render a valid award. (Final Award of October 16, 1999 in 15 Mealey's Int'l Arb. Rep. A1 (2000), para. 67)

It results from the above that the tribunal's discretion may be defined as the inherent power to preserve the integrity of the proceedings and to conduct them in an expeditious and effective manner so as to end the dispute between the parties by rendering a valid award. This is only a working definition subject to the usual caveat that any definition is dangerous (*omnis definitio in jure periculosa est*).

When does a tribunal have discretion?

This residual power finds its textual foothold in different provisions of the ICSID Convention containing the word "*may*" and, more generally, in Article 44 of the same instrument. Article 44 empowers a tribunal "to fill a specific gap regarding the conduct of specific proceedings." (*Abaclat et al. v. Argentina*, ICSID Case no. ARB/07/5, Decision on Jurisdiction August 4, 2011, para. 527) As the tribunal is *Abaclat et al. v. Argentina* explained:

> "Article 44 [is an] expression of the inherent power of any tribunal to resolve procedural questions in the event of **lacunae**.
> As a matter of principle, the power of a tribunal is **limited to the filling of gaps** left by the ICSID Convention and the Arbitration Rules. **In contrast, a modification of existing rules can only be effected subject to the parties' agreement**, in accordance with minimum standards of fair procedure and to the extent that the rules to be modified are not mandatory (in the sense that they restate mandatory provisions of the Convention).
> A tribunal's power is further limited to the filling of gaps left by the ICSID framework **in**

> **the specific proceedings at hand**, and a tribunal's role is not to complete or improve the ICSID framework in general. As such, a tribunal's power to fill gaps will usually be limited to the design of specific rules to deal with specific problems arising in the proceedings at hand." (paras. 521-523; emphasis added)

Consequently, a tribunal may utilize its discretionary authority on two occasions:
– if there is a permissive rule which uses language such as "*the tribunal may*";
– if the tribunal identifies a *lacunae* – according to Article 44.

Limits to arbitral discretion

It is said in the *Phoenix Action v. Czech Republic* case that "[t]here is nothing like a total discretion…" (ICSID Case no. ARB/06/5, Award of April 15, 2009, para. 82) But where do we find the limits of arbitral discretion? The only guidance coming from the ICSID practice is the case of *Corn Products International, Inc. v. United Mexican States*:

> "The Tribunal considers that the two principles by which it should be guided in the exercise of its discretion are (a) the efficient conduct of the proceedings and (b) fairness to both disputing parties." (ICSID Case no. ARB(AF)/04/01, Decision on responsibility 15 January 2008, para. 8)

Consequently, from Article 52(1)(d) of the ICSID Convention which relevantly mentions "*serious departure from a fundamental rule of procedure*" (a two-prong test) as a ground for annulment of awards the inference may be drawn that these fundamental rules are the outer limit of the tribunal's discretion. Such core rules are impartiality of the tribunal; equality of the parties; right to be heard; other. (Schreuer, C. et al., *The ICSID Convention: A Commentary* (Cambridge University Press, 2nd edn: 2009) at pp. 979-996) It follows that an ICSID tribunal retains a broad margin of discretion in the conduct of the proceedings subject to the observance of fundamental rules of procedure. (See Article 17(1) UNCITRAL Arbitration Rules as revised in 2010; See also Born, G., *Arbitral Tribunal's Discretion to Determine Arbitral Procedure* in Born, G., *International Commercial Arbitration* (Kluwer Law International: 2009) at p. 1762)

This is also confirmed by the *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. Argentina* annulment decision:

> "It is not for an annulment committee to second guess how a Tribunal exercises its discretion, unless a particular exercise of discretion amounts to a serious departure from a fundamental rule of procedure." (ICSID Case no. ARB/01/3, Decision on Annulment of July 30, 2010, para. 192)

Likewise, the committee in *Vivendi v. Argentina* second annulment recognized that "[procedural incidents may] be considered grounds for annulment. In the view of the *ad hoc* committee, they can but only if they rise to the exacting standards for annulment as expressed in Article 52(1)". (ICSID Case no. ARB/97/3, Decision on annulment, 10 August 2010, para. 251) This shall not mean that a tribunal is otherwise permitted to make 'trivial departures' from fundamental rules of procedure, but only that such errors will not amount to annullable defects.

Aside from the above, an arbitral tribunal enjoys a wide margin of discretion on issues of *quantum*.

(*Rumeli Telekom v. Kazakhstan*, ICSID Case no. ARB/05/16, Decision on Annulment March 25, 2010 at para. 146; *Wena v. Egypt*, supra, para. 91) As the tribunal in *Rumeli Telekom v. Kazakhstan* put it:

> "**The estimation of damages… is not an exact science**. It is of the essence of such an exercise that the tribunal has a measure of discretion, since the final figure must of its nature be an approximation of the claimant's loss." (Decision on Annulment, para. 179(5); emphasis added)
> "[T]he precise amount of this damage is a matter for the tribunal's informed estimation in the light of all the evidence available to it." (Id., para. 147)

A litigant's dissatisfaction with such estimation provides no ground for annulment. An annulment committee "is not a court of appeal, and that it is not the function of the Committee to pass judgment upon the substance of the Tribunal's decision with respect to the *quantum* of damages." (*Azurix Corp. v. Argentina*, ICSID Case no. ARB/01/12, Decision on annulment September 1, 2009, para. 362) As long as the tribunal has applied the proper law and has stated the reasons for its decision, no annullable defect will exists. Scholars reported that in the past, "on a number of occasions, tribunals appear to have simply 'split the baby', by taking the mean between alternative valuations produced by the parties…" (Ripinsky, S., *Assessing Damages in Investment Disputes: Practice in search of perfect* in 10:1 J. of World Inv. & Trade 5 (2009) at p.8) This is, so to say, part of the game since it must be recognized that:

> "When parties select arbitral rules, they incorporate by reference those rules and effectively grant arbitrators the discretion afforded under them. As a result, parties are generally precluded from later objecting to arbitrators' exercise of that discretion." (*US Restatement of the Law Third*, Council Draft No. 3, Reporters' notes at p. 230)

This part sought to throw light on the thorny question concerning the limits of arbitral discretion. The topic is important since arbitration in which the tribunal enjoys unfettered discretion is akin to an *expensive* Old Master picture without a proper frame. It may threaten the credibility of the ICSID system. Part II of this post will examine the issue of which actions can an arbitral tribunal take *proprio motu* as a special case of discretionary authority.