Kluwer Arbitration Blog

Are unilateral appointments defensible? On Jan Paulsson's Moral Hazard in International Arbitration

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In his April 2010 inaugural lecture as holder of the Michael R. Klein's Chair at the Miami University, Jan Paulsson advocated a fundamental change in the culture and practice of international commercial arbitration (Moral Hazard in International Arbitration, Miami, 29 April 2010, see also on this blog). In a nutshell, his views can be summarized as follows: contrary to a well established idea, there is no right of the parties to appoint arbitrators; quite to the opposite, the established practice of unilateral appointments is incompatible with the very concept of impartial dispute resolution, for a party cannot be expected to accept the legitimacy of an award rendered by its opponent's arbitrator. The concept of entirely impartial arbitration thus commands to "forbid, or at least rigorously police" the practice of unilateral appointments. All members of the arbitral tribunal should accordingly be appointed by a neutral body, which result can be achieved by establishing pre-existing lists of arbitrators or by using a variety of other list procedures.

There is of course plenty of anecdotal evidence that party-appointed arbitrators sometimes misbehave. Jan Paulsson cites the case of an arbitrator having communicated to his appointing party confidential information on the tribunal's deliberations, the apparently admitted bias of one of the arbitrators in the *Loewen* arbitration, and other examples. Yet, no sound case can only rest on examples. The broader picture is however, Paulsson argues, that party-appointed arbitrators generally lack impartiality. Evidence of that general situation of bias would be that dissenting opinions are almost invariably written by the arbitrator appointed by the losing party. What better evidence could there be that they systematically favor the side they owe their nomination to, and can therefore not be trusted for full impartiality? And what better demonstration could ever be found that the link between the arbitrator and his appointing party is the original sin that needs to be eradicated in order for arbitration to rise to the level of a fully impartial and trustworthy system of resolving disputes?

Jan Paulsson's proposal, of course, leads to displacing the perceived problem of bias from the individual appointees to the arbitral institutions: it is solely the inability to trust the arbitral institutions to appoint good arbitrators that would ultimately justify that parties retain control over the constitution of the arbitral tribunal; unfortunately, according to Jan Paulsson, "only a few arbitral institutions can make credible claims to legitimacy". As a consequence, "the organizations that call themselves arbitral institutions need to look at themselves and ask why it is that they are so exposed to suspicions of poor selection of arbitrators, and maybe even worse: cronyism and other forms of corruption".

Jan Paulsson's description of the arbitral institutional landscape is perhaps a bit harsh, but whatever the reality may be, he proposes no other solution than to "dismantle" the "empty edifices" that most arbitral institutions in his view are. Yet, this is not a result that is likely to be easily achieved. Arbitration is an opened and free market, and there is no regulatory authority that could grant arbitral institutions license to operate. In addition, any attempt to reach some sort of worldwide regulation of the way arbitral institutions appoint arbitrators – assuming that such a regulation could ever be achieved – would probably produce entirely undesirable results and ultimately be worse that the illness that it would be supposed to cure.

Arbitration offers a wide range of options to its users. Parties can retain full control over the arbitration by opting for ad hoc arbitration. They can also choose rules that allow them to appoint the arbitrators while ensuring some degree of control by the institution. Other institutions, like the LCIA, offer the kind of entirely neutral process in the constitution of the arbitral tribunal that Jan Paulsson advocates. Some, like the NAI, use in an effective manner list procedures to appoint all arbitrators in cooperation with the parties. The ICC is midway: the parties can appoint "their" arbitrator, but unless they agree on the contrary the chair will be appointed by the institution. Each institution has its own specificities, and is very much keen to maintain these differences as a means of identifying itself on a highly competitive market. Why should those differences disappear? This variety of offers is an advantage to the consumers of arbitration, provided they are well advised. The market will ultimately select the most efficient system.

The fact is that the market seems to have little appetite for a ban on unilateral appointments. Many institutional rules have been recently revised, and none moved from unilateral to institutional appointments. The ICC is currently revising its rules, and it is unlikely to apply to all arbitrators the current default rule providing for the chairperson's appointment by the ICC Court.

As said above, the ICC Rules provide that chairpersons are appointed by the institution. Yet, on the 337 chairs appointed in 2009, 21 were selected by the parties and 172 by the co-arbitrators, representing 57% of the total of appointments. The percentage of chairs appointed by the parties or the co-arbitrators (as opposed to those appointed by the Court) was 58.7% in 2007 and 57.3% in 2008. In almost 60% of the cases, the parties therefore agreed to depart from the default rule providing for an institutional appointment, which seems to indicate a strong willingness to retain some degree of control over the constitution of the arbitral tribunal.

The LCIA is equally interesting, as its rules provide for the appointment of all arbitrators by the LCIA Court. Its figures are all the more telling that the LCIA is well-known for the high quality of its appointments. During the course of 2009, the LCIA Court made a total of 502 individual appointments to a total of 220 tribunals. Of these 502 individual appointments, 199 were made by the parties, 54 chairs were appointed by the co-arbitrators, and the remaining 249 were made by the LCIA Court: in more than 50% of the cases, the parties thus agreed to depart from the institutional appointment in spite of the impeccable reputation of the institution.

It may well be that such a situation should be explained by comfort in the *status quo* rather than sound analysis by the parties of their genuine interests. And Jan Paulsson is certainly right in much of his criticism of unilateral appointments. It is true that many party-appointed arbitrators tend – in a more or less subtle manner – to favor their appointing party. It is also true that in extreme cases, partisan co-arbitrators *de facto* turn a three members tribunal into a one member tribunal in which the chair decides the award without listening to his colleagues. It is equally true that a higher lever of collegiality may be reached when all arbitrators have been appointed by a neutral body, thus

leading to an award of greater quality. And there are other potential advantages of all arbitrators being appointed by the institution, such as the ability to select individuals having special skills, such as engineers or accountants, to sit with lawyers in the tribunal.

The question, however, is whether banning unilateral appointments will increase the level of confidence by the parties in the arbitral process and contribute to improve the quality of arbitrators and awards.

It is often said that unilateral appointments contribute to the acceptance of arbitration by ensuring that the tribunal fully understands the culture of each party. Jan Paulsson is however correct in saying that cultural divides in arbitration have diminished and that parties now have significant common grounds in what they expect in the resolution of their dispute. In addition, arbitral institutions are perfectly capable of addressing that concern by appointing arbitrators from different cultures.

But unilateral appointments serve a broader purpose: by appointing an arbitrator, the parties – rightly or wrongly – get a sense of proximity with the process. Unilateral appointments give the parties the impression that they control the arbitration, and that is an important difference between arbitration and court litigation. The parties' trust in the arbitral process is not the arithmetical addition of each individual party's own trust in its own appointee; it is more a matter of collective trust in the system as a whole, a trust which rests on a variety of factors, amongst which the perception of proximity and control is an important one. From that perspective, little comparison can be drawn between arbitration and the experience of international courts.

It should also be borne in mind that by having each of them selecting an arbitrator, the parties manage to retain a high degree of control on the appointment of the decisive person, i.e. the chair. Most of the times (either because the applicable rules so provide or because the parties agree to derogate any rule on the contrary), chairpersons are appointed by the co-arbitrators or by the parties in consultation with the co-arbitrators. And it is generally accepted that, as an exception to the general prohibition of *ex parte* contacts with the parties, it is not improper for party-appointed arbitrators – provided of course all parties play by the same rules and that there is an appropriate level of transparency – to liaise with their appointing party as far as the appointment of the chair is concerned (and of course limited to such matter). Skilled arbitrators know how to manage the appointment process, in a more or less formal manner, in order to reach a result that will satisfy not only themselves, but also the parties and their counsels. And the possibility for each arbitrator to discuss the appointment of the chair with its appointing party is an essential element of the success of that process. In addition, a considerable amount of time is often devoted by party-appointed arbitrators to these consultations with the parties and their counsels, which institutions would not be able to do, at least not to the same extent. In sum, an institutional appointment is unlikely to be as consensual and satisfactory to all parties as one which is made as a result of a carefully tailored consultation process involving all participants.

A general ban on unilateral arbitration could have undesirable consequences. It could create a distance between the arbitral community and the users of arbitration. Arbitrators would look less at the parties and more at the institutions, which all have their own degree of internal politics and their bureaucracy. The risk would exist that arbitrators progressively move from their current culture of services providers, close to the needs and requirements of the users, to a culture of arbitral public servants or, even worse, of arbitral politicians. No one has to gain from such an evolution.

Ultimately, arbitration is only as good as the arbitrators are, and this principle also applies to party-appointed arbitrators. There is nowadays widespread awareness, amongst the users of arbitration, that hired guns do them more harm than good. Save in exceptional circumstances, whatever the perceived strengths of their case are, parties want to appoint arbitrators who will be listened and respected within the tribunal. And parties know that the standing and reputation of experienced international arbitrators depend from their capacity to exercise independent judgment when deliberating with their colleagues. As a consequence, party-appointed arbitrators tend to be selected more for their reputation of impartiality and integrity than for their supposed willingness to support their appointing party's thesis.

It is certainly true that party-appointed arbitrators often feel that they should do their best in order to make sure that the arguments of "their" party have been fully and seriously considered. But why should that be improper? The genuine dynamics of a well organized deliberation rests on the tribunal carefully analyzing each of the arguments raised by the parties, and it can only be beneficial to both parties that each arbitrator points to questions that may have been overlooked or insufficiently considered.

All this is not to say that that the current practice is totally immune from defects. It is true, as Jan Paulsson points outs, that unanimity awards are not always achieved in principled ways, and that tribunals sometimes attempt to compromise. But such instances are limited, and such compromises are generally reached on the allocation of costs, an area in which tribunals enjoy a fair level of discretion. It is also true that dissenting opinions are most of the times written by the arbitrator whose appointing party loses. But dissenting opinions are rare and most of the times self-contained. Jan Paulsson finally points to instances in which unscrupulous arbitrators offered iniquitous bargains in the tribunal's deliberations, but no general conclusion should be drawn from exceptional and highly reprehensible misconduct of that kind.

The true question is whether a party-appointed arbitrator is capable of exercising independent judgment. The answer is that experienced and reputable international arbitrators do. And if they don't, they quickly lose their reputation and cease to be interesting potential nominees for well advised parties. Certainly, many inexperienced arbitrators will not rise to that standard. But they do more harm to the parties which appoint them than to the system as a whole. The bottom line is that if parties really want to enhance their chances of success, they should appoint experienced, impartial, arbitrators rather than super-advocates. Jan Paulsson's proposal rests on the premise that parties are not capable of doing so. I believe, on the contrary, that the progresses of arbitral culture around the world commands a different answer; but the deepest values of international arbitration will not fully make their way in the business community if the users do not regard themselves as part and parcel of the system, something unilateral appointments greatly contribute to.

Ultimately, the problem of partisan arbitrators is more a survivance of progressively disappearing old misconceptions than the expression of structural faults of a dispute resolution system that is diverse and should remain so. Eliminating the evil of partisan arbitrators is more a matter for continuing education and dissemination of the international arbitration culture than for sweeping reforms such as a ban on unilateral appointments.

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This entry was posted on Tuesday, October 5th, 2010 at 3:42 pm and is filed under Arbitration Institutions and Rules, Arbitrators, Commercial Arbitration, Investment Arbitration
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