Kluwer Arbitration Blog

Would a 'Fair and Informed Observer' Really Agree With the Challenge Decision in Deutsche Lufthansa AG v. Bolivarian Republic of Venezuela?

Efemena Iluezi-Ogbaudu, Akriti Kataria · Monday, February 27th, 2023

On 10 October 2022, the Secretary-General of the Permanent Court of Arbitration ("PCA") accepted a challenge brought by Venezuela against the appointment of the Claimant's appointee, Dr. Wolfgang Peter, in an investor state arbitration (PCA Case No. 2022-03) instituted by German Claimant, Lufthansa ("Challenge Decision"). The Challenge Decision is the latest in the series of striking decisions impugning the independence and impartiality of an arbitrator based on previously expressed opinions. This decision is peculiar as it impugns the independence and impartiality of an arbitrator based on prior opinions expressed not by himself but by a different professionally-related arbitrator. Challenges of this nature have sparked intense debate within the academic community as well as among practitioners. Against this background, this post revisits the test for decisions on an arbitrator's independence and impartiality (previously discussed here), will submit that the challenge should have been decided differently, and advocate for a presumption of independence and impartiality in favour of arbitrators as a starting point in a process that necessarily requires a thorough factual analysis.

The PCA's Decision and The 'Fair & Informed Observer' Perspective

In the arbitration, Venezuela had raised concerns regarding Dr. Peter's independence and impartiality and challenged his appointment on two grounds [¶28 of the Challenge Decision]. First, that Dr. Peter could be influenced by the views of a senior colleague at his law firm, Prof. Tercier, who had acted as President in a dispute involving "*similar factual and legal issues*" (*Air Canada v. Venezuela*).

Second, that in Venezuela's view, it could not be ruled out that Dr. Peter and Prof. Tercier

> "*might exchange opinions, directly or indirectly, concerning the factual and legal circumstances of both cases*."

In accepting Venezuela's challenge, the PCA held that from the perspective of a

> "*reasonable, fair and informed third party, there is a clear risk that Dr. Peter might be influenced by factors other than the merits of the case*".

It came to this conclusion after noting that Dr. Peter's appointment "*would appear as more than a coincidence*" to a reasonable and informed third-party and

> "*would be perceived as being motivated by the influence that Prof. Tercier's decision…would hold for Dr Peter [who]…would potentially have to call into question the judgment of a close colleague in order to come to a different result on a substantially similar factual and legal pattern*".

In essence, the PCA was concerned that Dr. Peter would not have approached the issues in dispute impartially, but rather with a desire to conform to the views previously expressed by his "*close colleague*", Prof. Tercier in a different dispute. As demonstrated below, the propriety of this decision is doubtful given the almost universal principles on arbitrator challenges.

Test For Ascertaining Bias

The test for challenges requires a factual finding on the existence or otherwise of the likelihood of bias. This decision is an objective one that is to be made from the perspective of a fair, informed, and reasonable third-party, taking into consideration all relevant circumstances. This test is arguably uniform across procedural rules, in an overwhelming number of jurisdictions including the United Kingdom, France, and Switzerland and in investment arbitration jurisprudence. In the Challenge Decision, the parties and the PCA agreed to the application of this test [¶35 of the Challenge Decision]. To guarantee an objective decision, a factual analysis is necessarily required. A decision accepting a challenge must identify facts which give rise to justifiable doubts as to the arbitrator's independence and impartiality from a fair, informed, and reasonable third-party's perspective. This was not the case in the Challenge Decision. On the contrary, the facts do not support the PCA's conclusion.

Facts Do Not Support The Challenge Decision

The Challenge Decision essentially concludes that two well-reputed international arbitrators would be willing to violate their duties as arbitrators by exchanging confidential information concerning two separate arbitrations. This was despite Dr. Peter's restated commitment to his confidentiality obligation and duty to decide the dispute. The authors consider that, unless the PCA did not consider Dr. Peter's comments to be credible, which was not the case given its express comments to the contrary, a decision accepting the challenge to his appointment required more. As the Claimant pointed out, there was no proof of Dr. Peter's involvement in the Prof. Tercier arbitration or of the likelihood that Prof. Tercier and/or Dr. Peter would breach their duty of confidentiality.

The application of the test suggests that there is a gaping evidentiary hole in the Challenge Decision. It is doubtful that a fair and informed third-party observer, aware of the established

practices of lawyers and arbitrators, would conclude that an arbitrator would prejudge the issues in the arbitration in deference to a professional colleague, especially given that the business of the firm is not directly at stake in the arbitration. The suggestion that two practitioners, much less, senior practitioners cannot disagree respectfully should not be encouraged. Contrary to the impression this decision creates, lawyers, arbitrators, and national court judges disagree quite often.

It is also worth mentioning that the Challenge Decision's finding that Dr. Peter's appointment was not a "*mere coincidence*" has no bearing on his independence and impartiality. While exercising their right to appoint arbitrators, parties appoint those arbitrators who they think would appreciate the nuances of their dispute. This is part and parcel of arbitral practice and should not, in isolation, have any effect on an arbitrator's mandate.

Challenge Decision Wrongly Extends Issue Conflict to Prior Third-Party Opinions

The PCA rightfully characterised the Respondent's challenge as an issue conflict challenge despite the Respondent's attempt to characterise it differently [¶38 of the Challenge Decision]. Given this characterisation, it is noteworthy that all known issue-conflict decisions have considered the possible bias of an arbitrator based on their own previously expressed opinions. The Challenge Decision extends the scope of possible issue conflicts by upholding the challenge based on a third-party's prior opinion. This is an obvious cause of concern given the resultant risks identified in other similar decisions.

Considering the risk of upholding issue conflict challenges, the challenge decision in *Electrabel* v. *Hungary* [¶41] notes that investor–state and commercial arbitrations would become unworkable if an arbitrator were disqualified on the sole grounds that he or she has been exposed to similar legal or factual issues in concurrent or consecutive arbitrations. This risk is even more present if arbitrators are disqualified on the ground that an indeterminate group of persons considered "*close colleagues*" had dealt with similar legal or factual issues in prior arbitrations. This significantly reduces the pool of arbitrators available for appointment and threatens the integrity of arbitration as a whole.

The unchallenged members in the *Suez/Vivendi v. Argentine Republic* [¶36] challenge decision also sounded a word of caution in this respect. They specifically noted that:

> "*A finding of an arbitrator's or a judge's lack of impartiality requires far stronger evidence than that such arbitrator participated in a unanimous decision with two other arbitrators in a case in which a party in that case is currently a party in a case being held by that arbitrator. To hold otherwise would have serious negative consequences for any adjudicatory system.*"

The High Threshold For Issue Conflict Cases Not Met

Another consequence of the PCA's characterisation of the challenge as an issue conflict is that it

reveals the Challenge Decision's disregard for the high threshold required for issue conflict challenges in existing arbitral literature and jurisprudence. As a starting point, the IBA Guidelines on Conflict of Interest (Green list item 4.1.1) do not consider an issue conflict to be problematic, placing it on its green list. Similarly, challenges of this nature have been upheld sparingly, and only in cases where exceptional circumstances existed. For example, the challenge decision in *CC Devas* v. *India* [¶64] disqualified Prof. Orrego Vicuna not just because of his previous position in three decisions, but because he further defended his position in an academic publication after these decisions were annulled by three different ICSID annulment committees. No similar additional circumstances exist in the Challenge Decision.

Conclusion – A Presumption in Favour of an Arbitrator's Independence and Impartiality

Arbitration, in any form, presents a promise of neutral, independent, and impartial adjudication of disputes that should not be contradicted by decisions like this one. Unless circumstances exist to clearly suggest a likelihood of bias, an arbitrator's independence and impartiality should not be open to question. Despite the objective nature of the bias test, soft law, and existing jurisprudence lending credence to this position, challenges of this nature continue to abound and decisions like this one remain a possibility. These decisions further perpetuate the concerns of those who strongly oppose the continuance of the investor state dispute settlement regime.

To reduce the risk of similar future decisions, the authors recommend the recognition of an evidentiary presumption in favour of arbitrators' independence and impartiality. This will necessarily see arbitrators deemed independent and impartial unless and until the challenging party establishes facts to rebut the presumption with concrete evidence to the contrary. The authors do not consider this as an articulation of a new principle, but rather a reconceptualisation of the existing position. The present framework on challenges already assumes an arbitrator's independence and impartiality until a challenge is made. When a challenge is made, a finding of bias can only be made after an objective assessment based on factual circumstances. This is analogous to how a presumption operates. For issue conflict cases in particular, the emphasis on a high threshold in the jurisprudence, like a presumption, ensures a bias assessment starts off with the arbitrator's presumed independence and impartiality. While recognising that a presumption does not alter the test, the authors hope it alters its application to ensure similar decisions are avoided.

This entry was posted on Monday, February 27th, 2023 at 8:41 am and is filed under Arbitrator Bias, Arbitrator Challenges, Conflicts of interest, IBA Guidelines on Conflicts of Interest, Independence and Impartiality, Permanent Court of Arbitration
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.