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IN FOCUS

INT'L ARBITRATION

Now getting longer and more costly

Process is criticized for the same failings as litigation, but there are ways to manage costs.

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INTERNATIONAL ARBITRATION—once heralded as a more effective and efficient alternative dispute resolution mechanism than international litigation—is now routinely criticized for replicating some of the same failings as litigation: excessive cost and duration of proceedings.

The greatest strength of international arbitration—its procedural flexibility—can be used to control its increasing cost and duration. As a party or practitioner, the key is choosing the best procedural tradeoffs to maximize the ability to present one's strongest case without incurring unnecessary and substantial additional costs or time.

Nearly 40% of in-house counsel reported in a 2006 PricewaterhouseCoopers study that, in their experience, international arbitration was more expensive than international litigation. The study, by Gerry Lagerberg of PricewaterhouseCoopers and Loukas Mistelis

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of Queen Mary's School of International Arbitration, entitled "International Arbitration: Corporate Attitudes and Practices 2006," states that half of the in-house counsel respondents named "expense" as their greatest concern with international arbitration. See www.pwcadvisory.co.jp/common/media/International%20Arbitration.pdf.

The increased expenses and delays associated with international arbitration observed by in-house counsel have been confirmed by outside counsel. For example, in June 2008, Chambers USA reported that the leading international arbitration practitioners in the United States agreed that "it would be misleading to suggest that [international] arbitration is the cheaper or faster option" than litigation. Chambers & Partners USA, Chambers Commentary—International Arbitration, Overview (2008), www.chambersandpartners.com/usa/resultseditorial.aspx?cid=618&pid=20&solbar1&grouptype=2&FullOv=1.

Understandably, businesses and their counsel are comparing the benefits and drawbacks of international arbitration against those of international litigation. In the 2006 PricewaterhouseCoopers survey, only 11% of respondents indicated their preference for international litigation over international arbitration. A June 2008 PricewaterhouseCoopers survey of the same title, however, found that 44% of participating in-house counsel stated they "mostly used" international arbitration, while 41% "mostly used" transnational litigation. See Lagerberg and Mistelis, "International Arbitration: Corporate Attitudes and Practices 2008,"

at 5, www.pwc.co.uk/pdf/PwC_International_Arbitration_2008.pdf?utr=1.

Despite this growing recognition of the heightened costs of international arbitration, it does not appear that counsel or their clients are prepared to abandon it. In 2006, 95% of in-house counsel reported to PricewaterhouseCoopers that they would continue to use international arbitration. In the 2008 PricewaterhouseCoopers survey, 86% of respondents indicated that they were satisfied with international arbitration due to the enforceability of arbitral awards, the flexibility of procedures and the ability to select arbitrators. The 5% of respondents who reported that they were "rather" or "very" disappointed with international arbitration, however, cited increased costs and delays.

Sophisticated businesses will not countenance their counsel's complacency in controlling costs and fees. Because international arbitration will remain an important mechanism for resolving international disputes, counsel and their clients have a strong interest in adopting tactics that will keep time and costs to a minimum.

Rising costs and duration

A critical reason for rising costs is the increased size and complexity of disputes submitted to international arbitration. For example, the 2005 and 2007 Arbitration Scorecards published by *American Lawyer's Focus Europe*, an affiliate of *The National Law Journal*, surveyed the world's largest commercial and investment arbitrations. These surveys reported that the number of arbitrations

worth \$1 billion or more increased from 42 in 2005 to 63 in 2007—an increase of 50% in just two years. The increased size and complexity of disputes directly affects the cost and duration of arbitration proceedings. Michael Goldhaber, “Sneak Peek,” Focus Europe, June 2005, at S22; Michael Goldhaber, “Houston, We Have an Arbitration,” Focus Europe, June 2007, at S16.

In arbitration, costs essentially stem from five sources: arbitral institutions, arbitrators, experts, counsel and the arbitration process itself. Although the first two sources are unique to arbitration, the last three are sources of costs in litigation, as well. However, the flexibility of arbitration permits parties to manage costs by selecting the features that they value most.

■ *Administrative fees for arbitral institutions.* Administrative costs consist of an institution’s administrative fees and expenses connected with the hearings themselves. Although these fees and expenses comprise a relatively small amount of the total cost of international arbitration, there is no material counterpart in litigation.

Clients frequently ask which institution is cheapest. There often is not a clear answer, however, because an institution’s administrative fees depends on the calculation method used by that arbitral institution, which usually involves discretionary factors.

The majority of leading international arbitral institutions, including the International Chamber of Commerce (ICC) and the American Arbitration Association’s International Centre for Dispute Resolution, calculate administrative fees on the ad valorem method, namely, as a percentage of the amount in dispute, but subject to a cap. Under this approach, larger claims for damages translate into increased administrative expenses until the maximum is reached. The London Court of International Arbitration (LCIA) likewise charges a flat registration fee, but calculates other administrative costs according to the amount of time spent by the institution’s registrar and secretariat in administering the particular arbitration.

Businesses may avoid institutional fees by electing ad hoc arbitration, in which the arbitrators administer the arbitration by themselves. However, ad hoc

arbitration is not necessarily a cheaper option, for several reasons. First, most experienced arbitrators still prefer institutional assistance in administering even ad hoc arbitrations.

Second, if one party refuses to arbitrate, costs and time accumulate far more quickly in an ad hoc arbitration than in an administered arbitration, particularly in international disputes.

Third, under the United Nations Commission on International Trade Law arbitration rules, which are the leading set of rules for international ad hoc arbitrations, the arbitral tribunal is

As in U.S. courts, experts now routinely testify.

permitted to fix its own fees for its work. Consequently, tribunals constituted under ad hoc arbitration rules generally charge hourly fees for administrative activities, which is likely to be more expensive than the methods used by a particular arbitral institution.

■ *Arbitrators.* International arbitrators’ fees can comprise a considerable portion of arbitration costs. Comparing the cost of arbitrators is difficult because arbitrators—and arbitral institutions—employ different compensation rates and methods. Some arbitral institutions, such as the ICC, use a variation of the ad valorem method, in which the size, complexity and time necessary to reach an award are the basis for arbitrators’ fees. Other arbitral institutions, such as the LCIA, allow arbitrators to charge an hourly fee of up to 350 pounds an hour.

One or three arbitrators?

The most important factor is whether to appoint one or three arbitrators. This decision, like other tradeoffs that parties must make, centers on one’s view of risk: whether the cost and time necessary to appoint and receive an award from three arbitrators is outweighed by the likelihood that a sole arbitrator could commit a material error that prejudices the party. Routine disputes with, for example,

less than \$5 million at stake probably justify only a single arbitrator. However, if a relatively low-value dispute involves a politically or economically sensitive issue, three arbitrators may provide the party with more confidence.

A similar cost-benefit analysis may be conducted with respect to the situs, or seat, of the international arbitration. The most desirable situs are usually in cities where the courts are stable and commercially minded. These also tend to be the most expensive cities in the world. Parties seeking cost savings, however, may hold hearings in a location cheaper and more convenient than the location they selected as situs, as permitted under all of the major international arbitration rules.

■ *Experts.* As the complexity and size of international arbitrations has increased, so has the amount of money that parties expend to retain experts. As in U.S. courts, experts in international arbitrations now routinely testify regarding commercial, regulatory and industry practices; foreign and international law; and damages.

Expert witness costs could, of course, be eliminated if parties and their counsel decided against using them. However, that is unlikely, given the predilection of litigators to seek advantage for their client.

■ *Counsel.* The increased costs for counsel in recent years result from increased legal fees and increasingly complex arbitration procedures. The increased amount and complexity of disputes drive counsel to spare little cost in advancing their client’s position, and counsel costs correlate to the arbitral process.

■ *The arbitration process.* One of the most significant causes of increased cost and duration of international arbitration is the adoption of procedures that are characteristic of U.S. litigation. Recent years have seen the growth in the number of parties (actual or implied), broader and more numerous document or discovery requests and parties’ increased willingness to challenge awards.

First, as international disputes become more complex, the inclusion of multiple parties may be necessary or appropriate. If an underlying contract (or contracts) contains or implicates multiple parties, a dispute may arise as to

whether those parties should be joined in the arbitration, and, once joined, how multiple parties will proceed. If arbitrations are not consolidated, then parallel arbitrations are likely. These issues may be litigated in local courts or decided by arbitral tribunals themselves; even that determination, however, is frequently the subject of dispute.

Second, accompanying the increased size and complexity of disputes is the now ubiquitous use of e-mail and other electronic documents for conducting every aspect of international business. International arbitral tribunals increasingly will be required, on a case-by-case basis, to evaluate and apply principles and procedures of electronic discovery to document retention, identification, collection and production. What principles and procedures will evolve—and whether they will look anything like those adopted by U.S. courts—remains to be seen.

In addition, when arbitrations are conducted in more than one language or documents must be translated, each step of the document collection, review and exchange process becomes more expensive. More documents exponentially increase the time and cost for translation, both for the attorneys collecting and producing them as well as for the attorneys, experts and arbitrators reviewing them.

Third, parties are increasingly more likely to appeal an adverse arbitral award to a local or foreign court. For example, as a review of reported cases demonstrates, the last decade has seen more than a threefold increase in the number of arbitral awards that have been challenged in U.S. courts under the Federal Arbitration Act (FAA), the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) or the Inter-American Convention on International Commercial Arbitration (collectively, Title 9 of the U.S. Code). If one examines only New York Convention cases, that threefold increase becomes a sixfold increase.

The U.S. Supreme Court's March decision in *Hall Street Associates LLC v. Mat-tel Inc.*, 128 S. Ct. 1396 (2008), which held that the scope of judicial review of arbitral awards is exclusively determined

by the FAA, effectively nullifies any provision in parties' contracts that provides for expanded or narrowed judicial review of arbitral awards under Title 9. *Hall Street's* elimination of the option for expanded judicial review will likely reduce court challenges to arbitral awards, although the viability of the "manifest disregard" standard itself will have to be settled first in U.S. courts unless Congress intervenes.

Cost, duration can be controlled at time of contract formation.

Management principles

The most effective way to control costs and the duration of any international dispute resolution mechanism is to evaluate, at the time of contract formation, the costs the parties are willing to incur and whether litigation or arbitration will achieve more cheaply and quickly their legal and business objectives. Unfortunately, many counsel and their clients repeat the mistakes of their predecessors by copying and pasting ambiguous or flawed arbitration or choice-of-court clauses into their contracts.

If parties choose international arbitration, they may begin—but should not end—with a model arbitration clause. Model clauses that clearly set forth the basics (agreement to arbitrate, applicable rules, number of arbitrators, situs and governing law) help prevent eventual unnecessary disputes over ambiguous or inaccurate language. However, parties should always adapt arbitration clauses to their specific needs and objectives.

Parties should critically assess, on a case-by-case basis, how to control the cost and duration of the arbitration. A 2007 report from the ICC's Commission on Arbitration entitled *Techniques for Controlling Time and Costs in Arbitration* provides a specific and comprehensive list of proposals for attorneys and arbitrators to consider in "shap[ing] the arbitral proceedings so that the duration and cost of the arbitration are commen-

surate with what is at stake in the case and appropriate in light of the claims and issues presented." See www.iccwbo.org/uploadedFiles/TimeCost_E.pdf. Suggestions include considering fast-track procedures or other time limits, expediting the arbitrator selection process, dispensing with various procedural requirements, using technology to reduce costs, limiting written submissions, minimizing document exchange/discovery, eliminating expert evidence, streamlining hearings and allocating costs to encourage efficient conduct.

Finally, although qualified international mediators are relatively scarce, parties increasingly are turning to mediation and conciliation as alternatives to resolving disputes before international arbitral tribunals. Mediation and conciliation now are routinely proposed by many international arbitral institutions, a number of which also possess rules that parties may incorporate into their contracts or adopt after a dispute arises. As the costs and duration of most international arbitrations continue to look less "alternative," the future will see a corresponding rise of a skilled group of international mediators to assist in quickly and effectively resolving international disputes. **NLJ**