# *Varia*

## *Leveraging the Arbitral Process to Encourage Settlement: Some Practical and Legal Issues*

Ugo DRAETTA

Professor of International Law
Catholic University of Milan *

*Sumario*: I. Introduction. II. Prearbitration settlement negotiations. III. Settlement by the parties during the arbitration proceeding. 1. The motivations to start the arbitration and their impact on settlement. 2. Factors affecting chances of settlement during the arbitration proceeding. 3. The provisions posted in the company's books and their impact on the chances of a settlement. IV. Role of Arbitrators with Regard to a Settlement and Related Issues. 1. How the arbitration process may indirectly facilitate settlement. 2. A direct role of the arbitrators in facilitating settlement. V. Recommendations and Conclusions.

### I. Introduction

It is a general feeling among practitioners that international commercial arbitration proceedings are becoming increasingly long and costly. This is due to many factors, including the rising size and more complex nature of the disputes brought to arbitration, a sometimes excessive proceduralization due to arbitrator fears of an award being challenged on due process grounds, the huge amount of documents which often have to be produced, and toleration of delaying tactics adopted by defendants. In addition, there is a relative scarcity of international arbitrators capable of effectively managing and controlling the process, thus handling complex cases without unnecessary delays. The arbitrators who meet these requirements are often too busy, which is one of the most frequent causes of undue delays and with respect to which arbitral institutions should be encouraged to play a more active role in reducing. Some practitioners openly speak, in this respect, of a "crisis" of the arbitration[1], which crisis, admittedly, is to a certain extent due to the enormous success of arbitration among its users in recent years. Also many corporate counsels express their concerns about the effective functioning of arbitration and propose various sets of remedies[2].

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[1] *Vid., v.gr.*, D.W. Rivkin, "Towards a New Paradigm in International Arbitration: The Town Elder Model Revisited", *Arb. Int'l*, 2008, 377: "if we continue as is, the system may eventually collapse under its own weight".

[2] With particular reference to construction arbitration, *vid.* P. Hobeck, V. Mahnken & M. Koebke, "Time for Woolf Reforms in International Construction Arbitration", *Int. ALR.*, 2008, 87–95. The authors, senior in–house counsels at Siemens AG, see the risk that arbitration in the construction

As a consequence, it is often difficult for the parties to avoid excessive delays and costs when an international commercial arbitration proceeding is carried through the final stage of the issuance of an award, let alone to predict the amount of such delays and costs. A termination of the dispute through an amicable settlement, even due to frustration with the proceedings[3], thus becomes the most effective way to reduce costs and delays of the arbitration proceeding and a desirable objective. To the extent international commercial arbitration can offer a positive climate which can induce the parties to a settlement, this will certainly enhance its credibility and effectiveness[4].

In addition, the settlement possibly reached by the parties may, if the parties so request, be recorded as an award on agreed terms, or a consent award, as specifically contemplated by the rules of certain arbitral institutions or applicable laws[5]. This will give to the agreement of the parties all the benefits of an arbitral award, in terms of enforcement and recognition[6].

The observations which follow are offered in this context. Though we are aware of the recent efforts aimed at using the arbitration proceeding in conjunction with other processes to achieve efficient and cost effective outco-

industry, because of rising costs and delays, becomes progressively marginalized by the dominance of other ADR techniques, in spite of their inherent limitations, and state that, within the Siemens group, the policy has been adopted of treating arbitration as a last resort for dispute settlement.... an alarming red flag. It must also be said, for the sake of the truth, that delays and costs in construction arbitrations are often due to the fact that arbitration, as and of itself, is not always the optimal means of resolving disputes in complex international construction cases, because of the unsolvable problems raised by the links often existing between the contract submitted to arbitration and other contracts: *vid.* U. Draetta, "Arbitration in international construction contracts: selected practical problems", *Les Cahiers de l'Arbitrage*, n. 2008/4, 13–22. Along the same lines, and on a more general basis, see the very interesting considerations and suggestions by the senior GE litigation counsel M. McIlwrath, "Ignoring the Elephant in the Room: International Arbitration: Corporate Attitudes and Practices 2008", *Arbitration*, 74, 2008, pp. 424–428.

[3] Examples of arbitrations settled out of frustration are given by M. McIlwrath, R. Schroeder, "The View from an International Arbitration Customer: in Dire Need of Early Resolution", *Arbitration*, 74, 2008, pp. 3–11, section 4.

[4] *Vid.* the very convincing considerations recently made by D.W. Rivkin, "Towards a New Paradigm in International Arbitration: The Town Elder Model Revisited", *Arb. Int'l*, 2008, pp. 375 ff. As a remedy to the perceived crisis of arbitration, the author advocates a more proactive role of arbitrators in facilitating a settlement between the parties, suggesting a return to basics and the adoption of what he calls the "Town Elder model". The techniques suggested by the author, within the context of this model, to speed up the process and facilitate a settlement, are mostly reflected in the considerations made under IV below.

[5] Art. 26 ICC Rules; Art. 26.8 LCIA Rules; art. 30 Uncitral Model Law; sect. 51 UK Arbitration Act 1996.

[6] The arbitrators, however, may refuse to issue an award on agreed terms if the agreement reached by the parties is contrary to public policy. For an accurate analysis of this kind of awards and their implications and limitations, *vid.* J.–M. Tchakoua, "The status of the arbitral award by consent: the limits of a useful ruse", *RDAI/IBLJ*, 2002, 775 ff.; M. Darmon *et alia*, "La rédaction des sentences dans le cadre d'arbitrage selon le réglement de la CCI", *Bull. de la Cour international d'arbitrage de la CCI*, vol. 16/n. 2, 2005, 42–44; M. Dolmans, J. Grierson, "L'arbitrage et la modernisation du droit communautaire de la concurrence", *Bull. de la Cour international d'arbitrage de la CCI*, vol. 14/n. 2, 2003, 50. *Vid.* also, for a comprehensive analysis of this topic, R.H. Kreindler, "Aspects of Illegality in the Formation and Performance of Contracts", *International Council for Commercial Arbitration Congress Series*, La Haya, 11, 2003.

mes, as a way to enhance settlement capabilities in international arbitration, we will not directly address this new notion of combining adjudication and settlement process ("MedArb" or "ArbMed")[7]. We will concentrate only on some legal and practical issues affecting the chances of reaching the settlement of a dispute likely to be submitted, or already submitted to a traditional arbitration proceeding, which is meant to remain as such, without changing its nature into that of a mediation or conciliation process.

## II. Prearbitration settlement negotiations

Though the subject of this analysis is settlement during arbitration, we will take the liberty of briefly mentioning one recurring issue related to prearbitration settlement efforts.

It is a common experience that the parties do not always exhaust all their chances to reach a settlement before resorting to arbitration, nevertheless they often try to do so. In this connection, frequently the parties document their settlement negotiations through minutes of meetings or other non binding precontractual documents, such as letters of intent or memoranda of understanding.

Though these documents are generally meant to remain confidential, occasionally the party which has an interest in showing how much of its position the other party was ready to give away will produce them in the ensuing arbitration proceeding. The other party may complain and raise objections and even successfully so but nonetheless the arbitral tribunal becomes aware of the negotiations and may unavoidably remain consciously or unconsciously influenced by their development, even if negotiations failed and no agreement was reached in the end. It is also possible, however, that an arbitral tribunal will consider that the party making a settlement offer will have acted reasonably and will use it in its determination of costs.

The key message for the parties and their counsels is, consequently, to pay special attention in documenting settlement efforts when there is the risk of an arbitration proceeding in case of failure of the negotiations. Each party should ask itself whether disclosure of these documents in the arbitration proceeding which could possibly follow would damage or benefit such party. In the first case, it would be wise not to document the settlement efforts. But parties rarely pay attention to these consequences, as practice shows, and arbitrators are often confronted with the developments of previous negotiations between the parties in an attempt to settle their dispute. This may not be a desirable outcome at least for one of the parties.

[7] For those who want to know more on this subject, we recommend reading the very interesting draft 2008 report of the CEDR (Centre for Effective Dispute Resolution) Commission on Settlement in International Arbitration, containing also a set of suggested Rules for the Facilitation of Settlement in International Arbitration: it can be found on www.cedr.com/arbitration (last visited on March 3, 2009).

## III. Settlement by the parties during the arbitration proceeding

*1. The motivations to start the arbitration and their impact on settlement*

The chances of a settlement between the parties during an arbitration are first of all affected by the motivations which lead the claimant to initiate the procedure. The decision to start an arbitration should in theory be taken by the claimant only after having exhausted all the chances for an amicable settlement and based on an objective evaluation of the merits of its own claim as well as an adequate risk assessment analysis. When this is the case, there is in general a better possibility for the parties to reach a settlement, once they, during the course of the proceedings, have had the chance to reassess the risk and better appreciate their respective positions.

However, there may be interpersonal factors which affect claimant's decision to start an arbitration, including difficulties in understanding the other side's behaviour because of cultural and language disparities, logistic problems or aggressiveness due to the interruption of sohappyonce commercial relationships.

Parties may be also driven by considerations not strictly related to the merits of the case. An arbitration may be started simply to show the other party that claimant is serious about its claims, in the expectation that it will be easier to reach a settlement after this seriousness becomes apparent to the other party through the request for arbitration. In other cases, there may be emotional factors playing a role in an arbitration strategy: high level management of the two parties may have had, for example, a confrontation and they may be led by the desire to assert their "ego", to protect their reputation or to be vindicated. In other cases, management may want to assert matters which it perceives being of "principle", whatever is meant by it. Similarly, individuals within an organisation may have their own jobs or reputations to protect, creating a powerful incentive against admitting any weaknesses in one's own case, and to convince other members of the organisation that blame is with the other side. All these motivations are of dubious value and will make any settlement effort much more difficult.

Whatever the strategic motivations, the reality is that, once the arbitration has been initiated, and the related costs start accruing, this has the effect of antagonizing the parties and the arbitration tends to take a life of its own. The actual decisionmakers tend to become uninterested in the developments of the proceeding leaving it to the lawyers, both inhouse and outside counsels, who end up taking the most active role. Particularly, in the case of outside lawyers, the latter tend to be more litigators than settlement negotiators, with a different set of objectives and related skills. Consequently, the strategy of commencing an arbitration as a way to induce the other party to a settlement, does not always pay off. However, if initiation of an arbitration as such rarely induces the other party to settle, some have observed that the settle-

ment rate tends to increase as proceedings evolve[8], though the scarce empirical evidence is at list mixed in this respect. As a matter of fact, an early settlement causes the largest savings for the parties, while a settlement at a later stage, conversely, can be favoured by the better chance the parties have had to evaluate the respective strengths and weaknesses and to anticipate the outcome of the arbitrators' potential decision. However, no precise empirical rule can be identified as to the optimal timing for a settlement during an arbitration proceeding.

As to the so called matters of "principle" which may lead a party to start an arbitration, though they may be understandable from an individual point of view, rarely they pay off in strict business terms. They tend to impair the objectivity of a party in making its decision, which should only be guided by the real business interest of the company acting as claimant, and often constitute a real obstacle to a settlement. There are indeed very few matters of "principle" for which is worth for a company to start a litigation. An individual, obviously, may have a different perception of what "matters of principle" even mean.

*2. Factors affecting chances of settlement during the arbitration proceeding*

If the parties were not able to settle the dispute between them before commencing arbitration, they should always try to reach, whenever possible, a mutually satisfactory settlement at any stage of the arbitration proceeding. A satisfactory settlement presents obvious advantages in terms of saving time and costs, as well as preserving good business relationships between the parties. However the practice shows that, although settlements during arbitration are frequent[9], they are not as frequent as they could be.

Factors which constitute obstacles to a settlement between the parties during an arbitration proceeding have been identified and analysed, utilizing empirical surveys which have recently being conducted[10]. Some of these factors are intuitive and include:

– *First move paralysis*. Both parties may hesitate in making the first move, fearing that it could be perceived by the other party as a sign of weakness.

–*Unrealistic expectations of outcome and/or costs of arbitration*. More importantly, at least one of the parties may have overoptimistic or otherwise unrealistic perceptions of its own chances of winning, coupled with an unreasonably low estimation of the arbitration costs and likely length of the

[8] C. Buering–Uhle, *Arbitration and Mediation in International Business*, Kluwer, 1996, p. 166.

[9] A. Bucher, *ASA Bulletin*, 1995, p. 568, estimates the settlement rate at approximately 50%, probably an overestimation.

[10] *Vid*. C. Buering–Uhle, *op. cit*., pp. 157 ff., and C. Buering–Uhle, L. Kirchhoff, G. Scherer, *Arbitration and Mediation in International Business*, Second edition, Kluwer, 2006, pp. 105 ff. The authors conducted two empirical surveys, one in 1991/1992 and one in 2001/2004. The two surveys dealt with, among other topics, the capacity of international commercial arbitration to facilitate voluntary settlement and the role the arbitrators play in this context. Settlement rate is estimated by them at 43% on average.

proceeding. In particular, the parties may undervalue the amount of internal resources, other than lawyers, needed for the successful conduct of a long arbitration (in terms of employees, witnesses and experts), and they may fail to consider all the difficulties associated with maintaining these resources available. For example, in the course of the arbitration proceeding, these people, who were originally knowledgeable about the underlying contract or project, may have moved to other positions, left the company and, in some cases, may have even joined the counterpart.

– *Absence of decisionmaker involvement*. Lack of involvement by a party's senior management in settlement attempts can cause a party to overlook its real underlying long term business interests and leave to lawyers to concentrate on reconstructing past events rather than building towards the future. This can be particularly unfortunate where the parties have the possibility of a commercial relationship that will be damaged by their adversarial positioning in arbitration.

– *Lawyers as a wrong interface for settlement*. Those conducting an arbitration may simply not have appropriate skills as negotiators necessary to reach a settlement. In extreme cases, this may be coupled with a lack of real interest in settling, especially by outside lawyers, who may have a financial interest in seeing the arbitration continue. Whether this gives rise to an unconscious bias in favour of continuing the proceedings when a settlement might be possible, or an unprofessional (and unethical) conscious effort to keep the dispute alive, may be impossible to discern.

– *Internal restrictions on settlement authority*. In certain situations, parties are under pressure not to make concessions and not to settle for less than 100% of their claim for fear of being criticized by board members or shareholders; in the case of public entities (or companies controlled by state ministries) in particular, there may be the additional fear of being accused of corruption or of not having adequately protected the public assets. For the parties which are in these situations, a final award is better than any settlement, even if such settlement could possibly end up being more advantageous for them.

– *Desire for legallybinding resolution*. In some cases a party may have a need for a final legal resolution of a disputed issues. For example, an arbitral decision, as opposed to a settlement, may be needed to satisfy the requirements of a loan agreement, an insurance agreement or a bankruptcy procedure. In addition, some parties may want an award at any cost, in order to "establish a precedent".

Appreciating and overcoming these obstacles, whenever possible, to a more realistic assessment about the outcome of the arbitration proceeding is the main task of a responsible party and of its counsel. Appropriate performance of this task will enormously increase the chances of a settlement, with the related savings in terms of costs and delays.

*3. The provisions posted in the company's books and their impact on the chances of a settlement*

For companies subject to accounting requirements and periodic external audits, there may be a further dynamic that influences or impedes an ability to reach settlement: provisions for disputes. When an arbitration proceeding starts, and while it is pending, the financial officers of the two parties are required to insert, and periodically update, a provision in the company books which is either a contingent liability or a contingent asset depending on whether the party is respondent or claimant. This is a requirement of sound accounting practices as well as of applicable accounting standards (such as the EU International Financial Reporting Standards or the US Generally Accepted Accounting Principles[11]) which often have the force of law, particularly for listed companies. The determination of the amount of these provision is a crucial management decision, which ought to be taken based on a realistic risk assessment, with the objective support of the inhouse and/or outside counsel. A prudent and conservative approach with respect to contingent liabilities is appropriate, although setting aside a provision that is too conservative in good times (only to be released back to profits in a business downcycle) may be a form of accounting gamesmanship frowned upon by auditors. As to provisions for contingent assets, prudence would dictate that these should either be avoided altogether or inserted only after a final arbitral award.

However, there is a certain amount of discretionary judgement in determining the amount of the provision, and it is not infrequent that the decision is affected by considerations unrelated to the merits of the claim or counterclaim.

There may indeed be some internal management dynamics which may lead to behaviours not entirely meeting the standard of honesty. It may happen that some manager simply made a mistake in conducting the underlying business relation with the counterpart, and that this mistake is at the core of the arbitration proceeding initiated. Such manager may be reluctant or unable to admit such mistake. This admission would in fact have negative effects on the manager's career and compensation. For example a sale manager, who has to meet his sale budget, may tend to unreasonably insist for the existence of a sale contract when no agreement was in fact reached. Hence, the decision to start an arbitration and to put the entire amount of the claim as a contingent asset, or to resist an arbitration and to put an inadequate provision as a contingent liability, in both cases in order to cover the mistake and delay the moment of the truth.

The mistake may have also been made by the lawyer who drafted the contract which is brought to arbitration. This mistake may be of legaltechnical

[11] The GAAP applicable standard for setting litigation risk reserves is Financial Accounting Standard 5, or FAS 5. Under FAS 5 a pending or threatened litigation must be disclosed on a company's financial statement if it is "reasonably possible" that there will be a loss.

nature, such as the insertion of an applicable law provision without having fully appreciated the consequences of such insertion. The lawyer, especially if inhouse counsel, may be reluctant to admit the mistake to his/her manager. This attitude by counsel may equally lead to inadequate provisions posted in the company's books.

Apart from any such mistake, however, in extreme cases an unrealistic amount can be inserted as a provision in the company books also because of severe pressures on management to meet the company's goals, which management is unable or unwilling to resist.

In all these cases, the amount inserted in the company's books as a contingent asset or a contingent liability may be determined according to considerations other than a realistic and objective risk assessment and this constitutes a very real obstacle to any settlement effort. In fact, any amount lower than the contingent asset or higher than the contingent liability respectively posted would immediately cause the company to book a corresponding loss. In order to avoid showing a negative result to the board or to the shareholders, management will be, then, inclined to resist any settlement not corresponding to the unrealistic amount reserved in the books, wait until the arbitral award, and then blame the arbitrators for a wrong decision, if not attempting to set aside the award, thus further delaying the moment of the truth.

Conversely, an amount objectively identified in the company's books as contingent asset or contingent liability is the best factor which could favour a settlement. Actually, such objective determination implies as and of itself a predisposition to settle. Indeed, if the settlement is more or less in line with the amount provided for in the company's books, management may be inclined to close the matter and save further costs and time.

It should also be mentioned that, though arbitral tribunals may be reluctant to accept a request from one party that the other party discloses the amounts reserved in its books, such amounts may be or become publicly available at least for listed companies [12].

The message for lawyers, especially inhouse counsels, is that they have the duty to do their best, in the interest of their clients, to make sure first of all that they are consulted as to the amounts to be reserved in the company's books (which is not always the case), so that the decision is not taken by the manager and the chief financial officer alone; secondly, they have to ensure that the abovementioned amounts correspond to a realistic risk assessment of the possible outcome of the dispute. This is crucial, though it may not always be easy for inhouse counsels to successfully fight internally to ensure that this objective is achieved. An author acutely observed that "a treache-

[12] Most listed companies disclose only a general reserve fund that is inclusive of all pending litigations, not reserves for specific disputes, although recent recommendations for accounting changes in the US (draft entitled "Disclosure of Certain Loss Contingencies, published on June 5, 2008 by the Financial Accounting Standards Board) have proposed that companies disclose with specificity as to each dispute for which a reserve is established.

rous dynamic ensues when the attorney is not critical enough of his client's expectations and both reinforce each other in their overconfidence"[13].

## IV. Role of Arbitrators with Regard to a Settlement and Related Issues

The main task of the arbitrators is to decide upon the issues submitted to arbitration. However, although facilitating a settlement is not the primary role of the arbitrators, no one would deny that voluntary settlement during the proceeding is for the parties a desirable objective, which should be shared and encouraged by the arbitrators. Actually, parties who see their arbitrators play an active role in helping them to reach an amicable settlement may leave the proceeding with a higher degree of satisfaction and a greater desire to resort to arbitration for future disputes, and this is likely to be the case with both parties, not just the perceived "winner".

Arbitration clauses themselves may require that the arbitrators act as settlement facilitators and certain rules of arbitral institutions, or applicable arbitration laws, expressly contemplate that the arbitrators may invite the parties to reach a settlement at any stage of the proceedings[14]. This is a reminiscence of the past tradition in many countries that arbitrators were expected to decide *ex aequo et bono* and facilitate a settlement between the parties.

Consequently, it can be generally stated that one of the goals of the arbitrators, even if not their primary goal, should be that of favouring and facilitating a settlement between the parties, whenever possible and subject to certain limits. German/Swiss practitioners tend to consider with particular favour a proactive role of the arbitrators in this direction[15], while AngloAmerican practitioners are more hesitant and lukewarm in this respect. However, the contrast is only apparent, as the AngloAmerican hesitations mainly focus on the potential risk of turning the arbitration proceeding into a mediation or conciliation process. This should be in general avoided or at least done

[13] C. Buering–Uhle, *op. cit.*, p. 175.

[14] Sect. 32.1 DIS Rules: "At every stage of the proceedings, the arbitral tribunal should seek to encourage an amicable settlement of the dispute or of individual issues in dispute"; Art. 25.1 of the Rules of the Chamber of National and International Arbitration of Milan: "At any moment in the proceedings, the Arbitral Tribunal may attempt conciliation between the parties". Here, however, the term "conciliation" is not a good translation of the Italian text, should not be understood in its strictly technical meaning and should rather be read and interpreted as "settlement". In addition, the arbitration laws of many countries encourage arbitrators to invite the parties to reach a settlement: for a complete list of such laws, see Appendix 4 of the abovementioned (note 7) draft 2008 report of the CEDR (Centre for Effective Dispute Resolution) Commission on Settlement in International Arbitration.

[15] *Vid.* H. Raeschke–Kessler, "The Arbitrator as Settlement Facilitator", *Arb. Int'l*, 2005, p. 525. The point of view of some German authors is best expressed by P. Hobeck, V. Mahnken, M. Koebke, "Time for Woolf Reforms in International Construction Arbitration", *Int. ALR.*, 2008, p. 92: "It is generally welcomed by companies if arbitration proceedings end through amicable settlement. The tribunal should be able to contribute to such an outcome. It is helpful for parties striving for amicable settlement if the arbitral tribunal – with the consent of both parties – informally reveals its own views on disputed issues or even makes its own proposals for a settlement – an approach which is not untypical in German proceedings".

with extreme caution, because of the inherent risk that the arbitrators loose their impartiality, should the mediation/conciliation fail, as it will be said later on.

*1. How the arbitration process may indirectly facilitate settlement*

First of all, the arbitrators can create an amicable and rational climate aimed at indirectly facilitating a settlement between the parties through efficient case management and control. Actually this is considered the noble office (*nobile officium*) of the arbitrators, particularly in the German/Swiss arbitration practice[16]. To this effect, the arbitrators may inject some realism into the parties expectations through several means, for example by asking appropriate questions on key points, by telling the parties what critical issues really matter or by asking senior decisionmakers to appear at the hearings. This way of managing the case may induce each of the parties to look with more respect, or at least attention, to the position of the other party, and not simply brush it aside. The various means available to arbitrators to achieve this goal include the following:

– *Efficient organization of proceedings*. Arbitrators can, and should, indirectly favour a settlement by the way they organize the proceeding. For example, if there are preliminary issues of legal nature, such as the determination of the jurisdiction of the arbitral tribunal, the applicable law or the legal qualification of a given contract, the arbitrators, by the way they conduct the hearings, may want to make sure that the legal consequences of the opposing positions are fully understood by the parties. In addition, these legal issues could be preliminarily decided through a partial award. This could lead the parties to a better risk assessment regarding the validity of their claims or counterclaims, which in turn may lead to an early settlement between them. The same is generally true with regard to the preliminary identification and/or resolution of any other factual issue, which the arbitrators consider particularly relevant and material to the outcome of the dispute[17]. One author has emphatically advocated that early disposal of patently unmeritorious claims or preliminary claimvetting might offer commercial arbitration a "fasttrack" back to its roots[18].

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[16] H. Raeschke–Kessler, *loc. cit*., p. 527.

[17] This course of action is suggested, in particular, by the Preamble No. 3 of the IBA Rules on the Taking of Evidence: "Each Arbitral Tribunal is encouraged to identify to the Parties, as soon as it considers it to be appropriate, the issues that it may regard as relevant and material to the outcome of the case, including issues where a preliminary determination may be appropriate". Along the same lines, AAA International Arbitration Rules, rule 16, provides that the arbitrators may "direct the parties to focus the presentations on issues the decision of which could dispose of all or part of the case". *Vid.* also Canon I of the AAA–ABA Code of Ethics or Arbitrators in Commercial Disputes, of March 2004.

[18] A. Goldsmith, Trans–Global Petroleum: "Rare Bird" or Significant Step in the Development of Early Merits–Based Claim–Vetting?, 26 *ASA Bulletin* 4/2008, 667–686, at 669. The author, taking as his point of departure the recent decision under ICSID Rule 41(5) in Trans–Global Petroleum, Inc. v. The Hashemite Kingdom of Jordan, the first ever rendered under this 2006 amendment to the ICSID Rules, identifies a broader jurisprudence of claim–vetting in treaty–based and commercial arbitration

– *Bifurcation where appropriate*. Along the same lines identified above, alternatively the arbitration proceeding could be bifurcated, if the arbitrators consider this an efficient way of managing the case. In a Phase I the most important claims and/or those capable of early resolution could be examined and adjudicated and a Phase II could be devoted to the remaining small claims (this is appropriate particularly in construction arbitrations, where the parties tend to file many claims, some of which of small value). The Phase I award may lead the parties to settle on the claims which should be the subject of the Phase II proceeding, thus avoiding such proceeding all together.

– *Managing witnesses to promote agreement on factual issues*. In addition, the arbitrators may suggest that the technical experts appointed by the parties meet among themselves, without the presence of the parties and their lawyers, and come back to the arbitral tribunal with a report stating the points on which, on a mere technical ground, they agree and the points on which they disagree, stating the reasons for their possible disagreement. When not influenced by the parties or their lawyers, technical experts tend to find a consensus between themselves more often than it is believed, as they value their reputation in the technical community and would hesitate in taking positions not sustainable from a technical viewpoint. Such common position of the technical experts may go a long way towards inducing the parties to a settlement.

– *Managing documentation*. Finally, in the exercise of their power of control and management of the case, the arbitrators may exclude the appearance of witnesses or experts at a hearing, if they consider such appearance irrelevant or immaterial on the basis of the written submissions of the parties. Art. 8.1 of the IBA Rules on the Taking of Evidence is explicit in this respect[19]. This conduct may avoid unnecessary delays, save costs to the parties and send them a strong message which could allow them to make a better assessment as to the outcome of the case in view of a possible settlement.

*2. A direct role of the arbitrators in facilitating settlement*

Arbitrators can take a proactive role in facilitating settlement, to various degrees of intensity. They may, first of all, as said before, expressly invite the parties at any stage of the proceeding attempt settlement, as sometimes it is even required by the arbitration clause or contemplated by the applicable arbitration rules or national arbitration laws[20]. They do not need the consent of the parties to act in this way and it is fair to say that the arbitrators should

and considers different approaches to adjudicating challenges to claims alleged to be "manifestly without legal merit".

[19] "The Arbitral Tribunal shall at any time have complete control over the Evidentiary Hearing. The Arbitral Tribunal may limit or exclude any question to, answer by or appearance of a witness..., if it considers such question, answer or appearance to be irrelevant, immaterial, burdensome, duplicative ...".

[20] *Vid. supra*, note 14.

always make an attempt in this direction as a general rule. The parties would often take very seriously an invitation by the arbitral tribunal to try a settlement and will exhaust their chances of reaching it probably to a better degree than they may have done prior to commencing the arbitration.

A more intense involvement by the arbitrators in facilitating a settlement could theoretically push them to adopt one or more of the following techniques: (*a*) offering to the parties their preliminary views as to the outcome of the case; (*b*) directly participating in settlement negotiations; (*c*) proposing a settlement formula; (*d*) meeting with the parties separately (caucusing) to discuss settlement; (*e*) arranging an agenda for settlement negotiations. In general, it can be said that a more proactive and direct role by the arbitrators in facilitating settlement negotiations is viewed with more favour in the German/Swiss arbitration practice than in US or UK arbitration practice.

The adoption of such more proactive techniques by the arbitrators in facilitating a settlement requires however an increasing degree of caution on their part, as there are two risks that the arbitrators have always to keep in mind and avoid: (*a*) they cannot turn themselves into mediators or conciliators, and (*b*) they cannot loose their impartiality, otherwise they may be disqualified or be driven to resignation. The two risks are related, as it is by acting as mediators or conciliators that the arbitrators mostly risk loosing their impartiality[21].

By impartiality we refer to the attitude of the arbitrators toward the subject matter of the case. It is a notion not necessarily coinciding with their independence or neutrality, which have to do with the relations between the arbitrators and the parties. To give an example, if arbitrators take part in settlement negotiations and such negotiations fail, they have to a certain extent given up part of their intellectual liberty to decide the case, once they have expressed their position and given advice to the parties. In this connection, it must be considered that impartiality may be impaired not only because of what the arbitrators state, but also because of the information they may get from the parties during settlement negotiations. Such information, if the negotiations fail, may even unconscionably affect their decision making process. In addition, the arbitrators not only have to remain impartial, but have also to avoid the perception by one of the parties of having lost their impartiality[22].

The arbitrators generally need the consent of all the parties or their joint request before engaging in these more proactive techniques. It is true that arbitration is a private procedure governed to a large extent by the autonomy of the parties and that they are free, subject to certain limits, to determine

[21] In addition, as a practical consideration, arbitrators do not always possess the skills of a mediator and would tend to undertake an evaluative rather than a facilitative role when they engage in mediations, thus increasing all the risks mentioned above.

[22] The need for the arbitrators to "appear" to be impartial is emphasised by R.M. Mosk, T. Ginsburg, Becoming an international arbitrator: qualifications, disclosures, conduct and removal, in R. Rhoades, D.M. Kolkey and R. Chernick, *Practitioner's Handbook on International Arbitration and Mediation*, 2nd edition, JurisNet 2007, 357–360, with details on "suspect factors".

which role they want the arbitrators to take in a settlement process between them. Nevertheless, this autonomy cannot be pushed to the point of changing the nature of the arbitration into a mediation/conciliation process or impairing the impartiality of the arbitrators, because in either case one or both of the abovementioned risks would materialize. In particular, the consent by the parties for the arbitrators to engage in the above techniques should also include, as a protection for the arbitrators, the waiver by the parties to seek to disqualify the arbitrators if negotiations fail. However, it should be kept in mind that even such waiver may not be sufficient to insulate the arbitrators from the risk of having to resign for loss of their impartiality[23]. General Standard 4 (d) of the IBA Guidelines on Conflicts of Interest very appropriately underlines the need for extreme caution on the part of the arbitrators when assisting the parties in settlement negotiations, as well as the inherent risks for them of having in any case to resign[24].

A few considerations can be made with respect to each of the abovementioned techniques.

When, upon joint request of the parties, the arbitrators offer their preliminary views as to the outcome of the case at any stage of the proceeding[25], they obviously give the parties a strong incentive to settle. The later is the stage of the proceeding at which the preliminary views are offered, the stronger the incentive is, yet the lesser is the amount of cost and time saving for the parties.

Always upon request of the parties, the arbitrators together (or only the Chairman, or one or both of the coarbitrators) can directly participate in settlement negotiations, or even propose a settlement formula. These practices, however, are often discouraged[26], as they may turn the arbitrators into mediators or conciliators, a role that is inappropriate for them. In addition, there is the already mentioned risk that they would loose their impartiality in

[23] H. Raeschke–Kessler, *loc. cit.*, p. 527; C. Buering–Uhle, *op. cit.*, p. 209.

[24] It is worth quoting such General Standard 4 (d) in its entirety: "An arbitrator may assist the parties in reaching a settlement of the dispute at any stage of the proceedings. However, before doing so, the arbitrator should receive an express agreement by the parties that acting in such manner shall not disqualify the arbitrator from continuing to serve as arbitrator. Such express agreement shall be considered to be an effective waiver of any potential conflict of interests that may arise from the arbitrator's participation in such process or from information that the arbitrator may learn in the process. If the assistance by the arbitrator does not lead to final settlement of the case, the parties remain bound by their waiver. However, consistent with General Standard 2(a) and notwithstanding such agreement, the arbitrator shall resign if, as a consequence of his or her involvement in the settlement process, the arbitrator develops doubts as to his or her ability to remain impartial or independent in the future course of the arbitration proceedings".

[25] The joint request by the parties is a strict requirement in this respect; it does not appear appropriate for arbitrators who want to continue to be impartial, and be perceived as such, to hint upon the possible outcome of the case without such joint request: *vid.* H. Raeschke–Kessler, *loc. cit.*, p. 530.

[26] The AAA–ABA code of Ethics for Arbitrators of Commercial Disputes of March 2004 (Canon III.a and IV.H) expressly discourages the participation by a neutral arbitrator in settlement discussions between the parties, as well as any *ex parte* communications on the merits between the arbitrator and one party alone. Against *ex parte* communications, as a general rule, *vid.* also R.M. Mosk, T. Ginsburg, Becoming an international arbitrator: qualifications, disclosures, conduct and removal, in R. Rhoades, D.M. Kolkey and R. Chernick, *op. cit.*, pp. 379–380.

case of failure of the settlement negotiations. As a general rule, the more the arbitrators engage in the settlement process, the more the risk increases that they loose their impartiality because of the information they may gather in the process[27].

Finally, the arbitrators can consider meeting with the parties separately to discuss settlement. Caucusing, again, could be in theory done by the Chairman alone, by the coarbitrators separately or together, or by all arbitrators. However, apart from being often unnecessary and rarely practiced, this technique is discouraged by many[28], because, in addition to the extreme level of risk for the arbitrators involved of loosing their impartiality, it may violate the rules of due process, according to which each party has to hear what the other party has to say and have the opportunity to respond. Consequently it is not a technique which should be recommended.

## V. Recommendations and Conclusions

As a conclusion, the following recommendations and considerations can be offered.

Parties should exercise caution in documenting their prearbitration settlement efforts, as this documentation is often brought to the attention of the arbitrators, in case of an ensuing arbitration proceeding, by the party which has an interest in doing so.

An arbitration should be started only based on an objective risk assessment by claimant, with the help of responsible counsel. Adequate and realistic amounts have to be posted in the company books as contingent assets or liabilities. When this is the cases, the chances of a settlement during an arbitration proceeding increase exponentially.

Arbitrators have to efficiently manage the case with a view to create a positive climate for a settlement, by the way they organize the proceedings, identify the material issues at an early stage and conduct the hearings.

Arbitrators can and should always take an active role, by expressly encouraging the parties to reach a settlement at any stage of the proceeding.

Any more proactive role by the arbitrators in facilitating a settlement requires first of all the agreement of all the parties, or their joint request. In addition, arbitrators have to pay extreme attention not to loose their impartiality or credibility in the process and not to turn the arbitration into a me-

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[27] For the case in which arbitrators engage in quasi–mediation techniques for settling a case with the consent of the parties, *vid*. the interesting observations made by R.B Davidson, International Mediation Basics, in R. Rhoades, D.M. Kolkey and R. Chernick, *op. cit*., pp. 428–427. The author, though discouraging the practice, identifies twelve golden rules for arbitrators settling cases, with a view to minimize the inherent risks.

[28] *Vid*., *v.gr*., H. Raeschke–Kessler, *loc. cit*., p. 535; D.W. Rivkin, "Towards a New Paradigm in International Arbitration: The Town Elder Model Revisited", *Arb. Int'l*, 2008, p. 382. Even the abovementioned (note 7) draft 2008 report of the CEDR (Centre for Effective Dispute Resolution) Commission on Settlement in International Arbitration, and the enclosed set of suggested Rules for the Facilitation of Settlement in International Arbitration, expressly disallow caucusing.

diation or conciliations procedure. The risk is that the arbitrators may have to resign or the award itself may be successfully challenged in court by one of the parties. It should be remembered that arbitrators have credibility only until they loose it, and they loose it only once. Caucusing with the parties, finally, seems to be a technique to be generally avoided.

# *Controversias relativas a inversiones españolas en China: el arbitraje internacional derriba "la gran muralla"*

Enrique FERNÁNDEZ MASIÁ
Profesor Titular de Derecho internacional privado
Universidad de Castillala Mancha



## I. Introducción

1. China en el año 2007 arrebató a Alemania el tercer puesto de la economía mundial, creciendo el 13% su Producto Interior Bruto (PIB) hasta llegar a una cifra de 3,38 billones de dólares. Únicamente se sitúa ya por detrás de EE UU y Japón, y según los analistas económicos, si siguiese a niveles de crecimiento similares, sólo necesitará dos décadas para sustituir a Estados Unidos como la mayor economía del planeta[1]. No es de extrañar que con estos datos económicos y, a pesar de que el gigante asiático también se vaya a ver afectado por la recesión que a nivel mundial se está produciendo desde el año 2008, se pueda hablar del mercado chino como un mercado con las mayores oportunidades a nivel mundial para los inversores extranjeros[2]. Esta afirmación viene corroborada por el dato de que en la actualidad China es el país mayor receptor de inversión directa extranjera en el mundo.

[1] De acuerdo con los datos publicados por el periódico *El Economista*, 14 de enero de 2009.

[2] Sin embargo, no todo son atractivos para la inversión en China. Tal y como recoge A. Pastor Palomar, "Inversiones España–China bajo el nuevo APPRI 2005", *REEI*, nº 12, 2006, p. 3, varios problemas han sido apuntados en relación con el clima inversor en el gigante asiático: la alta intervención del gobierno mediante la propiedad de empresas en sectores estratégicos, la falta de transparencia, la corrupción, la arbitrariedad en la toma de decisiones por parte de las autoridades competentes, la falta de respeto de los contratos o el incumplimiento de las resoluciones judiciales, son cuestiones de indudable importancia que resaltan la necesidad de lograr una mayor seguridad jurídica para las inversiones extranjeras.