

Counting the costs of investment treaty arbitration

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The expense of bringing a treaty claim is a major concern for investors but the final allocation of costs in a case can be hard to predict. In a major survey, **Matthew Hodgson** of Allen & Overy in Prague examines the costs findings in over 200 cases and argues that more transparency on the subject is needed.

The impressive growth of investment treaty arbitration over the past 15 years shows few signs of exhaustion. In 2013, some 40 new ICSID cases were commenced, second only to 2012 when the figure was inflated by a flurry of claims against Venezuela. Meanwhile, the number of bilateral investment treaties in force continues to grow, and ground-breaking projects such as the EU-China and EU-US free trade agreements are in prospect.

The continued growth of investment treaty arbitration brings it into contact with new users. Other than certain states and a small number of multinational companies, few entities are frequent users of the system. The aim of this study is to shed empirical light on a subject of considerable interest to such users, namely the costs of the process, and to examine the propensity of tribunals to adjust costs one way or another. It also considers the substantive outcomes of proceedings.

The study involved a review of some 221 cases in which an award or decision was publicly available on 31 December 2012. After making other adjustments (including removing decisions reserving costs to a later stage of proceedings), the final data pool was 176 cases.

Costs

The costs of an investment treaty arbitration fall into two broad categories. First, there are the fees and expenses of the arbitral tribunal itself, together with those of the institution or appointing authority, if any (tribunal costs). In addition, there are the fees and expenses of legal counsel as well as any expert or factual witnesses (party costs).

Party costs

The study revealed that the average party costs were quite similar, at US\$4,437,000 for claimants and US\$4,559,000 for respondents.

Actual party costs data for the claimant and respondent were available in 73 and 66 cases (out of the total pool of 176 cases) respectively. As a result of the relatively small data set, a few cases with extremely high costs distort the figures. The median result for claimants is somewhat lower at US\$3,145,000, whereas for respondents there is a much sharper drop to US\$2,286,000. These figures are perhaps more reflective of a typical mid-value claim.

The reason for this divergence is that in a number of cases the respondent's party costs were significantly greater than the claimant's. The most extreme examples are seen in the table below:

Table 1: Party costs – substantial discrepancies

Name of case	Respondent's party costs (US\$)	Claimant's party costs (US\$)	Discrepancy (US\$)
Jan Oostergetel and Theodora Laurentius v Slovakia	16,330,000	2,231,000	14,099,000
Libananco v Turkey	35,702,000	24,382,000	11,320,000
EDF v Romania	18,575,000	8,198,000	10,377,000

It is therefore clear that, excluding a number of extreme results, claimants typically incur considerably greater party costs than respondents. This is perhaps unsurprising since the claimant bears the burden of proof. Further, respondent states are generally more cost sensitive than claimants, with their tendency to run public tenders where price is the driving factor. Certain states also have in-house legal teams with substantial investment treaty arbitration experience. In some cases (for example, the US State Department) these legal teams directly represent the state in proceedings.

The study also confirmed that average party costs have increased over time, with a rise of 32 per cent in average party costs for claimants between cases decided before 2006 and those decided in or after 2006. However, a much sharper rise in the median (192 per cent) suggests that the rise in party costs for a representative “mid-value” claim might in fact be higher than this. Respondents have seen a similar average increase in party costs, with an average rise of 32 per cent for post-2006 claims. However, this represented a more modest 96 per cent rise in the median cost

Tribunal costs

Turning to tribunal costs, the study reveals that the average costs are US\$746,000 (median US\$590,000), or just over US\$373,200 for each party (split on a 50:50 basis). The pool of available cases was 70.

As with party costs, tribunal costs have also shown a noticeable increase over time, with average tribunal costs for 2006 and onwards 56 per cent higher than those before 2006.

Interestingly, the study revealed a disparity between tribunal costs depending on the forum.

Table 2: Average tribunal costs – UNCITRAL/ICSID comparison

Forum selected	Average tribunal costs (US\$)	Median tribunal cost
UNCITRAL	853,000	714,000
ICSID	769,000	544,000

The average tribunal costs in ICSID claims are 10 per cent lower than in an UNCITRAL claim. The median difference is nearly 24 per cent.

The obvious explanation for this is ICSID’s cap on arbitrators’ fees. The current schedule of fees (in force since 1 January 2008) states that, in addition to any direct expenses reasonably incurred, arbitrators are entitled to receive a fee of US\$3,000 a day for work performed in connection with the proceedings (together with a subsistence allowance where relevant).

By way of comparison, UNCITRAL has not historically had a similar fee cap, although the 2010 rules (article 41.4) now give the parties a right to appeal the tribunal’s fees to the appointing authority. The appointing authority has the power of adjustment of fees and expenses, which is binding on the tribunal. It remains to be seen whether these changes will reduce the discrepancy between tribunal costs in UNCITRAL and ICSID proceedings.

It should be noted that the average costs for the SCC were even lower at US\$480,000. However, the available data pool was considerably smaller (13 cases). Further, the

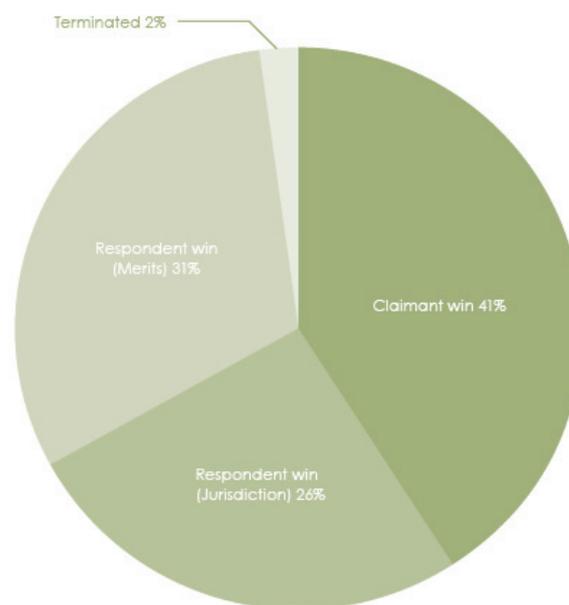
average amount claimed in SCC cases was much lower: approximately US\$92.2 million, as compared with an overall average of roughly US\$491.7 million. The SCC also provides for caps on the arbitrators' fees, scaled to the amount in dispute (although costs in cases worth over €100 million are decided by the SCC's board of directors on an individual basis).

Substantive outcome: who wins and how much?

The study also considered the relative success of claimants and respondents in relation to the substantive outcome. For simplicity, success was defined for the claimant as instances where it received an award of some amount in damages on the merits.

Across the full pool of 176 cases, respondents were successful in 59 per cent of cases. This is a sharp reversal from the initial trend in early investment treaty arbitrations: prior to 2001, investors prevailed in 63 per cent of cases.

Chart 1 – Substantive outcome



Of these, around 26 per cent of all cases (or nearly half of total respondent “wins”) were dismissed on jurisdiction. Some four cases (or around 2 per cent of the total) were terminated in circumstances where the claimant was ordered to contribute to the respondent’s party and tribunal costs.

In cases where the claimant was successful, the average amount awarded was US\$76,331,000. Again, the largest claims have a substantial distortive effect. The combined value of the awards in *Occidental Petroleum v Ecuador II*, *CSOB v Slovakia*, *CME v Czech Republic* and *Siemens v Argentina* alone was approximately US\$3.12 billion, exerting significant upward pressure on the average. The median

amount awarded was substantially lower at US\$10,694,000.

It is also interesting to consider the amount awarded in comparison to the amount claimed. In this regard, the study showed that on average a successful claimant was awarded 41 per cent of the amount it claimed. In just three cases out of the total 176 (CDC v Seychelles, Deutsche Bank v Sri Lanka and SGS v Paraguay) did the investor recover the full amount claimed.

Overall, the average amount claimed is US\$491,656,000. However, this figure conceals a notable discrepancy. A further breakdown reveals that in cases where the claimant is ultimately successful, the average amount claimed is US\$166,388,000, which is substantially lower than the average of US\$816,924,200 in cases where the claimant is unsuccessful. This suggests that the average amount claimed is greatly inflated by a number of flawed claims. The three unsuccessful cases in which the largest amounts were claimed are set out in the table below.

Table 3: Largest unsuccessful claims

Case	Amount claimed (US\$)
Saba Fakes v Turkey	19 billion
Libananco v Turkey	10.1 billion
Generation Ukraine v Ukraine	7.1 billion

Each of these awards involved misconduct, if not outright bad faith, by the claimant. Somewhat bizarrely, in *Generation Ukraine*, the claimant apparently sought to recover an alleged US\$2.3 billion in legal costs. Needless to say, this request, along with all claims, was rejected.

Apportioning costs

When it comes to the apportionment of costs there are two basic philosophies. The “pay your own way” principle suggests that a party should bear its own costs. Also known as the “American Rule”, this is the default position in US litigation and also in cases before the International Court of Justice. A number of investment treaty tribunals have endorsed this approach, for example, *Romak v Uzbekistan*, *MCI Power v Ecuador* and *Anderson v Costa Rica*.

In contrast, the “costs follow the event” or “loser pays” principle suggests that the successful party should ordinarily recover its reasonable costs. It is usual for a losing party to make at least some contribution to the costs of the winner in the national courts of many jurisdictions, including England & Wales, France, Germany, Hong Kong, Italy, the Netherlands, Poland, Russia, Singapore, Spain and Thailand. According to a 2012 study by Queen Mary, University of London, this approach is

common in commercial arbitration, being adopted in around one half of cases, with a further 30 per cent of cases seeing some apportionment of costs, leaving just 20 per cent of cases where costs were not adjusted. In the investment treaty arbitration context, it has found support, for example, in the decisions of *ADC v Hungary* and *Gemplus v Mexico*.

A third and more nuanced approach (really a variation on the “costs follow the event” principle) seeks to apportion costs based on the relative success of the different issues in the arbitration. Examples of this approach are the decisions in *Nagel v Czech Republic*, *International Thunderbird Gaming v Mexico*, *EDF v Romania*, *Occidental v Ecuador II*, and *Helnan v Egypt*. An unusual application of this “relative success” approach came in *Eastern Sugar v Czech Republic*, where the tribunal required the successful investor to pay part of the respondent’s share of tribunal costs (that is, ultimately “winner pays”), apparently on the basis that the claimant had submitted a large claim, of which it was awarded only around 25% in damages.

The ICSID Convention does not express a preference as between these approaches. Article 61(2) of the Convention leaves costs to the broad discretion of the tribunal, without offering an indication of the factors a tribunal may take into account in reaching its decision. An earlier draft of the Convention established a default “pay your own way” approach, except in the event of claims commenced “frivolously” or in “bad faith”. Ultimately, the question of costs was left entirely to the tribunal’s discretion.

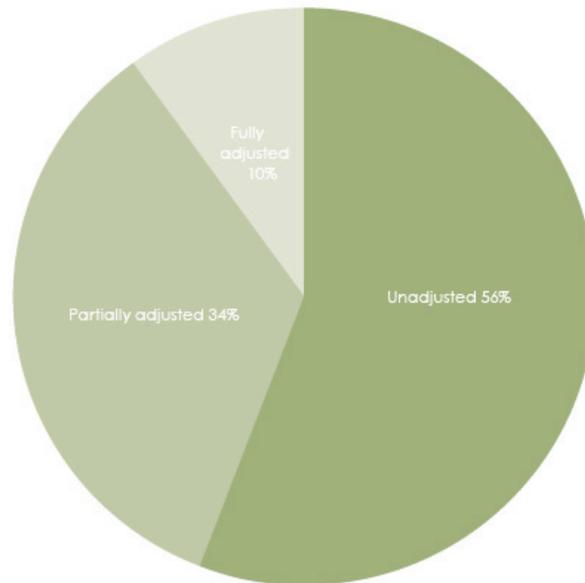
A different approach is taken in the 2010 UNCITRAL rules, which state at article 42.1 that “[t]he costs of the arbitration shall in principle be borne by the unsuccessful party or parties” subject to the proviso that “the arbitral tribunal may apportion each of such costs between the parties if it determines that apportionment is reasonable, taking into account the circumstances of the case”. The 1976 UNCITRAL rules contain similar, albeit more limited, provisions: article 40.1, which applies only to tribunal costs, and article 40.2, which expressly gives the tribunal discretion as to the party costs. As will be seen, this has led to divergent approaches between ICSID and UNCITRAL tribunals on the subject of costs.

Apportionment in practice

A tribunal has three basic options in terms of costs: to make each party responsible for its own party costs and 50 per cent of the tribunal costs (an unadjusted costs order); or to order one party to pay the other side’s party costs and tribunal costs in full (a fully adjusted costs order) or in part (a partially adjusted costs order).

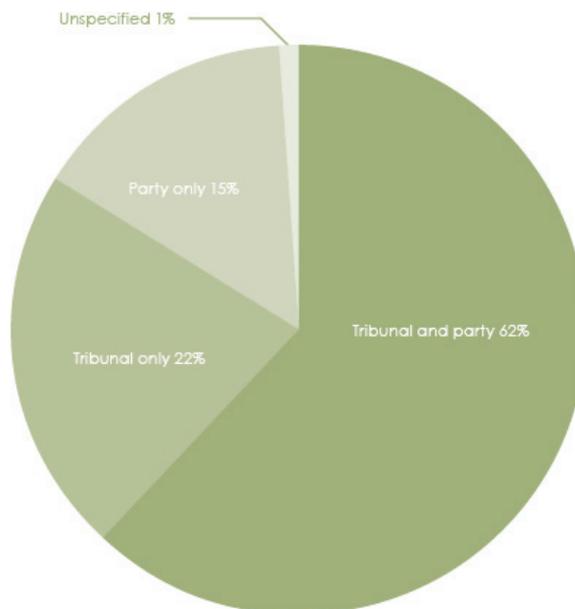
A slight majority of arbitration tribunals (56 per cent) have required each party to bear its own costs, that is, an unadjusted costs order. Just 10 per cent of tribunals made a fully adjusted costs order and 34 per cent a partially adjusted costs order.

Chart 2: Adjustment of costs



The chart below examines the ways in which tribunals elect to make an adjustment more closely. In nearly two-thirds of these cases, tribunals elected to adjust some portion of both tribunal and party costs. In the remaining cases, tribunals were more likely to make the adjustment to the tribunal costs, rather than the party costs.

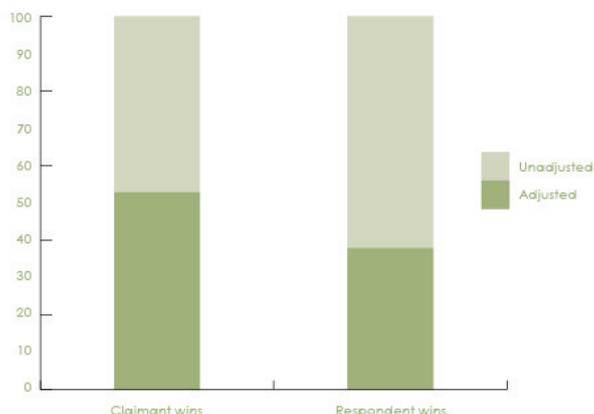
Chart 3: Breakdown of adjustments



Successful claimants are more likely to recover their costs than successful respondents. In a slight majority of cases (53 per cent), upon finding for the claimant, tribunals made an adjusted costs order. By comparison, tribunals make an adjusted costs order

in favour of a successful respondent in only 38 per cent of awards.

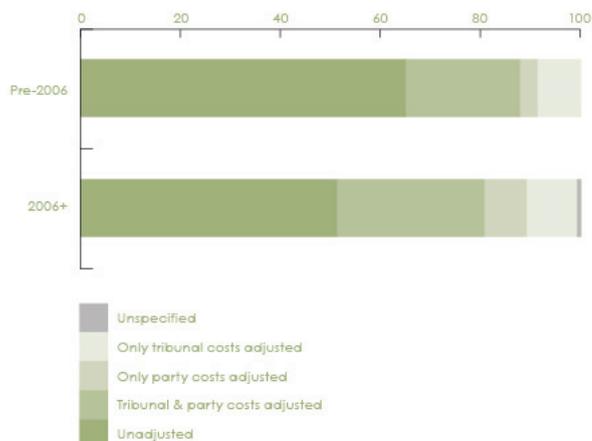
Chart 4: Adjustment of costs according to successful party



There are a number of possible explanations for this disparity. Where a claimant is successful, the tribunal has necessarily found an unlawful act by the respondent and, following the principles of compensation set out by the Permanent Court of International Justice in the *Chorzow Factory* case, may be mindful of the need to make whole the investor for losses flowing from the unlawful act. In contrast, where the respondent is successful, while concluding that it lacks jurisdiction or that there has been no technical breach of the relevant treaty, the tribunal may still perceive that the claimant has a legitimate grievance and was justified in pursuing the claim. An example of this was seen in *Azinian v Mexico*, where the tribunal, in finding for the respondent but making an unadjusted costs order, noted that the respondent “may be said to some extent to have invited litigation”. Similarly, the tribunal in *Salini v Jordan* noted that, while the claimant was unsuccessful, it remained sceptical of the respondent’s case.

It is a common perception among arbitration practitioners that investment tribunals are increasingly favouring the “cost follows the event” approach. The charts below show that this perception is justified. In awards decided before 2006, tribunals adjusted costs in just one-third of cases (35 per cent). However, in cases decided after 2006, this number has risen sharply and tribunals made some adjustment in around half (49 per cent) of awards.

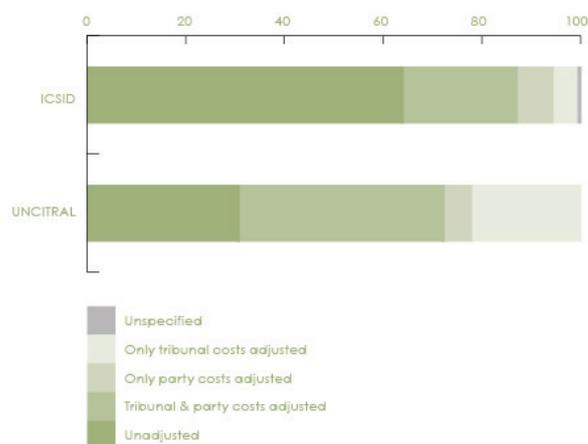
Chart 5: Adjustment of costs by date



There is a notable divergence between UNCITRAL and ICSID tribunals. In arbitrations conducted under UNCITRAL rules, tribunals made some form of adjusted costs order in over two-thirds (69 per cent) of cases, while ICSID tribunals only did so in just over one-third (36 per cent). This demonstrates the impact of guidance in the arbitral rules.

The UNCITRAL figures also reveal that tribunals adjusted both tribunal and party costs in 42 per cent of cases, adjusting only tribunal costs in just 22 per cent of awards. This is interesting because all cases surveyed were decided under the 1976 rules which, as set out above, provide guidance only with regard to the tribunal costs and expressly reserve the flexibility of the tribunal to award party costs as they consider appropriate. Yet despite this, UNCITRAL tribunals, when making an adjusted costs order, tended also to shift party costs.

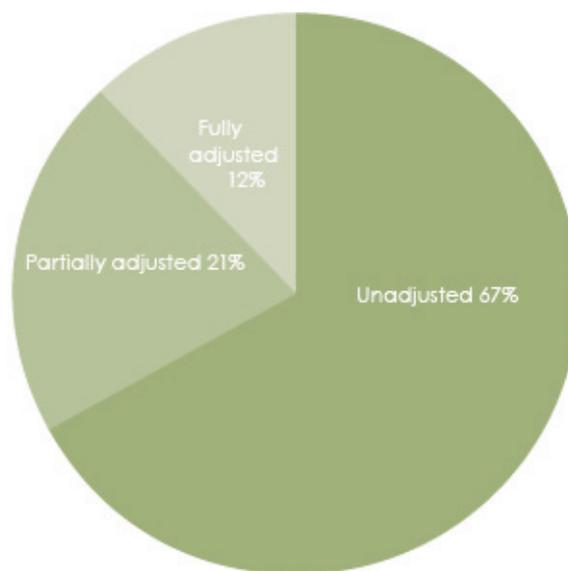
Chart 6: Adjustment of costs by institution



Annulment proceedings

The study also examined costs adjustment in the context of publicly available ICSID annulment decisions, with a total data pool of 24 annulment cases.

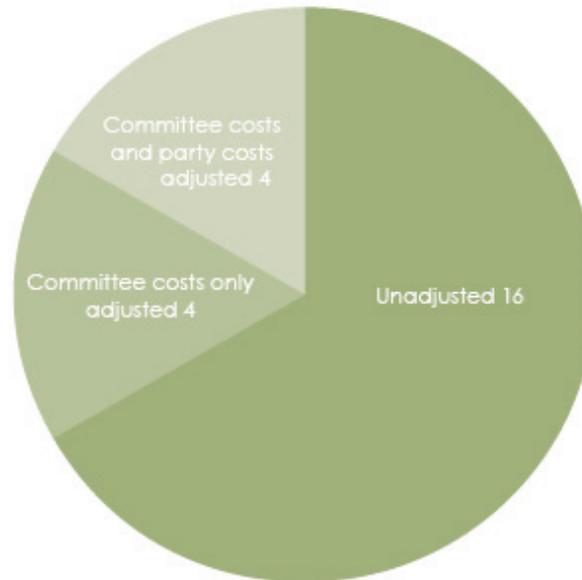
Chart 7: Adjustment of costs in ICSID annulment proceedings



Perhaps surprisingly, annulment committees show a greater tendency towards unadjusted costs orders than ordinary tribunals. In 16 cases (67 per cent of annulment decisions) there was an unadjusted costs order. Of the remaining eight decisions, some 21 per cent of the decisions made a partially adjusted costs order whereas just 12 per cent involved a fully adjusted costs order. Of these eight adjusted costs orders, four decisions involved an adjustment of the ad hoc committee's costs only, and four

decisions involved an adjustment of both the committee costs and party costs.

Chart 8: Breakdown of cost adjustments in ICSID annulment proceedings



In all six cases (25 per cent of annulment decisions) where the ad hoc committee decided to partially annul the tribunal’s award, there was no adjustment of either party costs or committee costs. In the five cases (21 per cent of decisions) in which the previous award was entirely annulled, there was no adjustment of party costs. However, the “losing” party was required to bear committee costs in two of those cases.

In the 13 cases (54 per cent of annulment decisions) where the application for annulment was dismissed, one might have expected tribunals more readily to require the unsuccessful applicant to bear the full costs of the process, consistent with the exceptional nature of annulment proceedings and the desire to discourage dilatory applications. However, of these 13 decisions, there were only three cases in which the committee made a fully adjusted costs order. There was no adjustment of party costs in 69 per cent of decisions where the application was dismissed. An adjustment of committee costs was made in 46 per cent of such cases.

It is interesting to note that the institutional appointment of the ad hoc committee does not increase their tendency to award costs to the successful party. Whereas the failure of tribunals to adopt a “costs follow the event” approach is sometimes attributed to compromises among arbitrators to maintain the unanimity of the tribunal, this does not appear to be borne out by the evidence.

A need for transparency

One of the challenges of conducting the underlying study is that full and clear costs information is provided only in a minority of cases. This is an area where, in the interests of transparency, there is room for improvement on the part of tribunals.

Despite the absence of full data, combining average party costs (for both parties) and average tribunal costs suggests a typical claim may cost in the region of US\$9,743,000; or, looking at the combined median figures, US\$6,021,000. Given that the average award is US\$76,331,000 (median US\$10,694,000) it is clear that costs are an important aspect of many proceedings. In cases where the respondent succeeds, costs will amount to the entire financial outcome of the dispute. At the same time, tribunals devote little attention to the subject, with just six paragraphs addressing costs in the average award.

The likely costs of a proceeding, and how these costs may be adjusted by a tribunal, are a part of the risk/reward assessment an investor makes before commencing an investment treaty case. It is also relevant to a state considering its approach to settlement discussions. As it stands, and notwithstanding the discernible shift towards “costs follow the event” approach in recent years, it is extremely difficult for parties to predict the approach a tribunal will take to costs. The UNCITRAL Rules at least provide guidance and a default position in this regard. However, the resulting divergence in approaches between ICSID and UNCITRAL tribunals is far from satisfactory.

I have argued elsewhere that the “costs follow the event” approach is an appropriate starting point in investment arbitration proceedings. One way to achieve this would be to amend the ICSID arbitration rules in line with the UNCITRAL rules. There are, of course, differing views on this and the debate is beyond the scope of this article. However, on any view, the allocation of costs is an important subject for the parties and deserves greater attention and a more principled approach from tribunals.

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