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Costs Allocation in Investor-State Arbitration

Wendy J. Miles

1. Introduction

It is now beyond serious debate that in the majority of international *commercial* arbitration cases, there is at least some costs allocation in favour of the successful party. This practice has emerged across commercial arbitration institutions, despite the fact that some of the major institutional rules contain no presumption whatsoever in favour of the successful party recovering its costs.

The purpose of this paper is to examine costs allocation in the specific context of investor-state arbitration. The author considers whether the growing acceptance and application of a presumption that the successful party is entitled to recover costs, including its legal costs, in international commercial arbitration should transcend into investor-state arbitration, either as a matter of practice or as a matter of policy.

Recently, various commentators have suggested that the same approach should indeed apply in investor-state arbitration.[1] However, there are a number of important factors to take into consideration. First, the limited publicly available investor-state arbitration information provides a tenuous basis for any broad, over-generalised conclusions concerning approaches to costs allocation. Secondly, that limited information reveals that it is not the approach in the majority of cases for investor-state tribunals to allocate costs to the successful party. Thirdly, the applicable procedural rules in investor-state arbitration generally do not incorporate a presumption that the successful party will recover its costs (although there are recent exceptions). Fourthly, the *travaux préparatoires* to the relevant treaties and rules generally support no such presumption. Finally, there are public policy arguments in favour of a continuing different approach to costs allocation in investor-state arbitration.

The absence of a presumption that a successful party is entitled to recover costs pursuant to costs allocation in investor-state arbitration is not necessarily inconsistent with the entitlement to full reparation pursuant to established principles of international law.[2] A wronged claimant still may be able, as far as possible, "to wipe out all of the consequences of the illegal act" by seeking to recover the cost of proceedings as part of its damages claim, subject to the ordinary standard of proof in damages. An advantage in the damages approach would be to avoid vague and inconsistent development of incoherent and disparate lines of reasoning (or lack of reasoning) that tend to emerge from costs decisions based on submissions by counsel made only after the conclusion of evidentiary hearings and oral argument on liability and damages, including after the conclusion of comprehensive expert evidence quantifying all other aspects of loss caused by the breach.

2. The Importance of Definitions and Terms

It is important to be clear and consistent in the use of certain terms and expressions in relation to costs allocation in international arbitration. Broad generalisations as to the purported existence of presumptions in respect of costs allocation sometimes fail to differentiate between the tribunal's treatment of "arbitration costs" and "legal costs" and can lead to misleading conclusions.

[1] M. Hodgson, "Costs in Investment Treaty Arbitration: The Case for Reform" (2014) 11(1) T.D.M., available at *http://www.allenovery.com/SiteCollectionDocuments/Costs%20in%20Investment%20Treaty%20Arbitration.pdf* [Accessed October 6, 2014] and C. Ong and M. O'Reilly, *Costs in International Arbitration* (Singapore: LexisNexis, 2013), p.203.

[2] *Chorzow Factory (Claim for Indemnity) (Merits), Germany v Poland*, 1928 P.C.I.J. Ser.A., No.17, Judgment No.13 (September 13, 1928).

Costs definitions in investor-state arbitration

Costs in investor-state arbitration—and most international arbitration—are generally divided into two main categories: "arbitration costs" (the costs of an arbitral institution and the arbitrators, including all tribunal fees and related administrative expenses), and "legal costs" (the parties' own costs, including lawyers' fees). Almost all procedural rules in investor-state proceedings distinguish between the two. In practice, tribunals have often treated them differently in their awards, sometimes allocating only "arbitration costs" and not "legal costs" to a successful party.

Article 61(2) of the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention) distinguishes between three types of cost: (i) "the expenses incurred by the parties in connection with the proceedings", (ii) "the fees and expenses of the members of the tribunal" (as defined in the ICSID Convention art.60), and (iii) "the charges for the use of the facilities of ICSID" (as defined in the ICSID Convention art.59).[3] The expenses incurred by the parties in connection with the proceedings consist primarily of their costs of legal representation.[4] These may also include the costs of in-house staff, accounting costs, expenses incurred in producing evidence and the costs of witnesses and experts presented by the parties.[5]

The 1976 Arbitration Rules of the United Nations Commission on International Trade Law (the 1976 UNCITRAL Rules) art.38 defines "costs" as:

> "includ[ing] *only*: (a) The fees of the arbitral tribunal …; (b) The travel and other expenses incurred by the arbitrators; (c) The costs of expert advice and of other assistance required by the arbitral tribunal; (d) The travel and other expenses of witnesses to the extent such expenses are approved by the arbitral tribunal; (e) The costs for legal representation and assistance *of the successful party if such costs were claimed during the arbitral proceedings*, and only to the extent that the arbitral tribunal determines that the amount of such costs is reasonable; (f) Any fees of the appointing authority as well as the expenses of the Secretary-General of the Permanent Court of Arbitration at The Hague."[6]

The 2010 UNCITRAL Rules art.40, which replaces art.38, broadens the definition of "costs" to include: (a) fees of the arbitral tribunal; (b) reasonable travel and other expenses incurred by the arbitrators; (c) reasonable costs of expert advice and of other assistance required by the arbitral tribunal; (d) reasonable travel and other expenses of witnesses to the extent such expenses are approved by the arbitral tribunal; (e) *legal and other costs incurred by the parties in relation to the arbitration to the extent that the arbitral tribunal determines that the amount of such costs is reasonable*; and (f) fees and expenses of the appointing authority as well as the fees and expenses of the Secretary-General of the PCA.

Costs presumptions in investor-state arbitration

Two broad approaches to allocation of costs have now emerged in international *commercial* arbitration: (i) that the successful party will be entitled to recover its costs; or (ii) that each party will bear its own costs. It appears to be the prevailing approach in most international commercial arbitration proceedings, irrespective of the administering arbitral institutions or applicable rules, that the successful party will recover at least some of its costs. The

[3] ICSID Convention Art.61(2).
[4] C. Schreuer, L. Malintoppi et al., *The ICSID Convention: A Commentary*, 2nd edn (Cambridge: Cambridge University Press, 2009), p.1227.
[5] L. Nurick, "Costs in International Arbitrations" (1992) 7 ICSID FILJ 57, 69.
[6] 1976 UNCITRAL Rules art.38 (emphasis added).

rationale for reimbursing the costs of the successful party is that it compensates that party and dissuades unmeritorious actions.[7]

In investor-state arbitration, this approach is sometimes also adopted, but it is far from becoming a generally accepted or prevailing practice.[8] It is particularly rare that a losing party in investor-state arbitration will be required to bear the entire burden of the prevailing party's legal expenses.[9] It remains the case that in the majority of investor-state arbitration awards, the tribunal requires the parties to bear their own costs.

Occasionally tribunals in investor-state arbitration do allocate costs for part of the proceedings or use costs allocation as a sanction for procedural misconduct.[10] For example, in some cases, tribunals awarded costs against a party as a sanction in cases of dilatory or otherwise improper conduct in the course of the proceedings.[11] In other cases, additional costs arose as a result of the respondents' non-participation and appropriate allocation was made.[12] Furthermore, the allocation of costs need not relate to the entire proceeding. The tribunal may impose upon one party the costs (or a major share of the costs) of a particular stage of the proceedings.[13] Often this will be in reaction to undesirable conduct by a party,[14] but more generally, a party whose conduct has necessitated a particular measure may be ordered to bear the attendant costs. For instance, if one party wishes the tribunal to visit a scene which is relevant in the dispute, the tribunal may elect to do so at the cost of the requesting party.[15]

As discussed below, there exists no presumption whatsoever in respect of costs pursuant to the ICSID Convention or Rules. Within the ICSID regime, costs are a matter solely for the discretion of the tribunal, be they arbitration costs or legal costs or both. Under the 1976 UNCITRAL Rules Art.40, there was a presumption that arbitration costs, in principle, would be borne by the unsuccessful party, but *not* the successful party's legal costs. Although that distinction was eliminated in the 2010 UNCITRAL Rules, as explained below, it remains to some extent in practice.

3. No Basis for "Presumption" in Investor-State Arbitration

Investor-state awards are unreliable—"precedent"

The legal principle of stare decisis requires judges to respect the precedent established by prior decisions. The principle originates from the Latin maxim "*Stare decisis et non quieta movere*" or "to stand by decisions and not disturb the undisturbed". The rationale for the principle is certainty and harmony in the development of the law.

Investor-state arbitration awards are subject to extensive analysis by scholars and practitioners in search of "norms" and "precedent" in numerous areas of substantive and procedural law in international arbitration. As a result of extensive empirical research and statistical analysis, some seek to identify principles and norms in order: (i) systematically to discern presumptions which form the basis of doctrine, policy, custom and practice and

[7] S. W. Schill, "Arbitration Risk and Effective Compliance—Cost-Shifting in Investment Treaty Arbitration" (2006) 7 J. World Investment & Trade 653, 665.

[8] N. Rubins, "The Allocation of Costs and Attorney's Fees in Investor-State Arbitration" (2003) 18 ICSID Review 127.

[9] Schreuer, Malintoppi et al., *The ICSID Convention: A Commentary*, 2nd edn (2009), p.1229.

[10] L. Nurick, "Costs in International Arbitration" (1992) 7 ICSID FILJ 57, 59–60.

[11] Schreuer, Malintoppi et al., *The ICSID Convention: A Commentary*, 2nd edn (2009), p.1230. See also N. Rubins, "The Allocation of Costs and Attorney's Fees in Investor-State Arbitration" (2003) 18 ICSID Review 127.

[12] See, e.g., *Benvenuti & Bonfant v Congo*, Award, August 15, 1980 at [4.124]–[4.129].

[13] ICSID Arbitration Rules art.28(1)(b): "(b) with respect to any part of the proceeding, that the related costs (as determined by the Secretary-General) shall be borne entirely or in a particular share by one of the parties."

[14] Schreuer, Malintoppi et al., *The ICSID Convention: A Commentary*, 2nd edn (2009), p.1231.

[15] ICSID Convention art.43(b).

to determine principles of international law; and (ii) to propose various measures for the prescription of a particular approach.[16]

The area of costs allocation in investor-state arbitration has not escaped such scrutiny, despite the power of arbitrators to allocate costs being procedural and almost entirely discretionary. Nevertheless, based on analysis of the limited universe of published prior awards, various commentators have recently suggested that the prevailing practice of allocating at least some costs to the successful party in international commercial arbitration applies, or at least should apply, also in investor-state arbitration.

The information upon which such conclusions are based is both incomplete and unreliable as a source of jurisprudential "precedent" for multiple independent reasons. In particular: (i) it excludes an unseen universe of unpublished and confidential investor-state awards; (ii) it excludes cases where parties may have independently reached an agreement in respect of costs; (iii) the published decisions frequently contain little or no reasoning in respect of the costs allocation decision; (iv) the published decisions often fail to reveal those factors that are truly determinative in the tribunal's cost decision; and (v) discussion often fails to distinguish between "legal costs" and "arbitration costs".

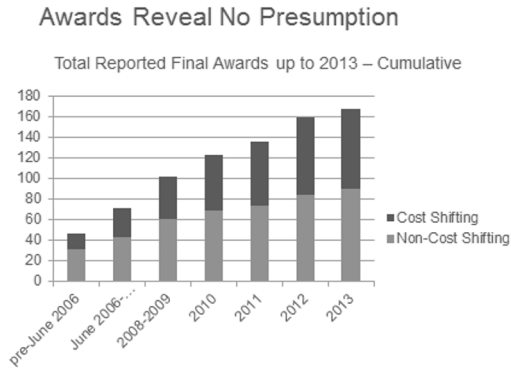
Moreover, the published decisions are rendered pursuant to different treaties and various arbitral rules, including but not limited to the ICSID Rules, the UNCITRAL Rules, the 2010 Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (the SCC Rules) and the Permanent Court of Arbitration Rules 2012 (the 2012 PCA Rules). These treaties and rules contain similar but often critically different provisions in relation to allocation of costs, as discussed below. Moreover, in certain cases costs allocation issues and approaches may be subject to separate agreement by the parties, including pursuant to treaty.

Existing unreliable "precedent" reveals no presumption

Despite limitations as a source of reliable "precedent", published investor-state awards dealing with costs allocation nevertheless reveal no presumption, preferred practice or trend at all. Instead they reveal that investor-state tribunals simply exercise their discretion on a case by case basis. There is no statistical support for the existence of a presumption that the successful party is entitled to recover its costs in investor-state arbitration, despite that undeniably being the case in the majority of international commercial arbitration awards. Indeed the publicly available information suggests instead that investor-state arbitration continues to "buck the trend on costs allocation": considerably less than half of the published awards have ever allocated any costs at all to the successful party.

A basic statistical analysis of 168 final arbitral awards addressing costs, rendered from 2006 to 2013, indicates that there is no trend in investor-state arbitral awards in favour of any particular approach to costs. The statistics demonstrate that less than half of unsuccessful parties were ordered to bear some part (but not necessarily all) of the successful party's costs and the remaining costs decisions, where one was taken, determined that each party would bear its own costs.

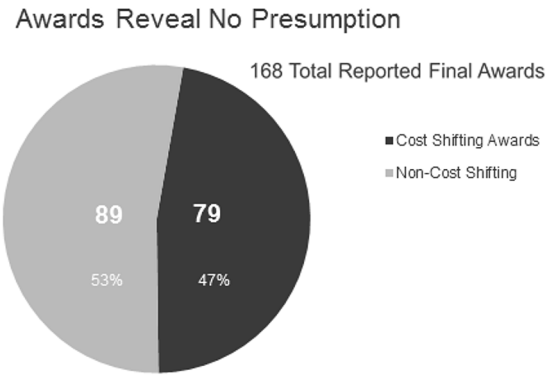
[16] D. Smith, "Shifting Sands: Cost-and-Fee Allocation in International Investment Arbitration" (2010–2011) 51 Va. J. Int'l L. 749, 776 (Smith argues that "some sort of certainty—imparted either via a bright-line costs rule or ad hoc interim rulings—would be beneficial"); S. W. Schill, "Arbitration Risk and Effective Compliance—Cost-Shifting in Investment Treaty Arbitration" (2006) 7 J. World Investment & Trade 653, 656 and 695 (Schill notes that "[i]n terms of legal certainty, it would … be desirable for States to clarify the basic approach to cost allocation they wish to endorse by including provisions in bilateral and multilateral investment treaties"); J. Y. Gotonda, "Awarding Costs and Attorneys' Fees in International Commercial Arbitrations" (1999) 21 Mich. J. Int'l L. 47–48 (Gotonda states that "[t]he current problems associated with the awarding of costs and attorneys' fees could be resolved by adopting the [American Rule]. … If adopted, the model will provide much needed uniformity and predictability to arbitral awards of costs and fees, while also ensuring that similarly situated parties are treated equally and fairly").



However such statistical analysis is based only on known cases and must therefore be treated with caution. Moreover, statistics derived from review of decisions on cost allocation often do not discriminate between parties' legal costs on the one hand and arbitration costs on the other.

The statistics show that there are a rapidly increasing number of decisions which address costs in some manner.[17] However, on a closer look, this increase simply reflects the more general trend of exponential growth in the number of investor-state claims and awards more generally. There is no marked change in the *proportion* of awards which address costs.

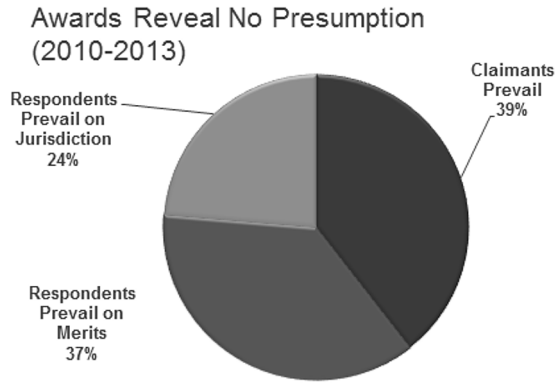
In analysing these cases, it was found that amongst these 168 final awards addressing costs to date, 79 shifted costs to the losing party and 89 did not, a 47 per cent to 53 per cent overall split in favour of each party bearing its own costs. There does appear to be a slight increase in the proportion of awards containing costs allocation in recent years. But this is only the case of those published final awards which contain a costs ruling, so excludes unpublished awards as well as published awards which resolve costs in some other manner.



Of those awards that shift at least some portion of costs to the unsuccessful party, these apportion more or less evenly between prevailing claimants and prevailing respondents. Prevailing claimants have recovered at least a portion of their costs in 39 per cent of the body of cost-shifting awards while prevailing respondents have so recovered in 37 per cent. The remaining 24 per cent comprises cases where the respondent recovered at least some portion of costs having prevailed on a jurisdictional challenge. It is evident that costs allocation following a successful jurisdictional challenge is statistically more likely in

[17] See United Nations Conference on Trade and Development IIA, Issues Note 1, May 2013, *Recent Developments in Investor-State Dispute Settlement*, updated for the Multilateral Dialogue on Investment, May 28–29, 2013.

proceedings under the UNCITRAL Rules than in those under the ICSID Rules (as discussed below). Furthermore, of this 24 per cent of published decisions on jurisdiction which have shifted at least some portion of the respondent's costs, none was rendered under the SCC Rules.



There is no marked change in the proportion of known arbitral awards which address the treatment of costs, and this existing body of awards is more or less evenly split as to whether the successful party will be entitled to recover *any* costs or these will be borne equally between the parties. There is simply no trend in favour of one or the other approach. In sum, the empirical data reveal no presumption as to allocation of costs in investment arbitration.

Applicable procedural rules reveal no presumption

In any event, in any international arbitration proceeding, one should look first and foremost to the parties' agreement in respect of costs allocation, rather than to statistical analysis of published awards. In investor-state arbitration, the relevant "agreement" is usually contained predominantly in the applicable treaty provisions and arbitration rules.

Many bilateral investment treaties (BITs) expressly state that parties will bear their own costs in state-to-state disputes arising thereunder; such state-to-state arbitral jurisdiction is typically restricted to those disputes regarding the interpretation or application of the BIT itself and is very rarely invoked. In investor-state disputes, BITs and other multilateral instruments are generally silent as to allocation of costs, but typically designate the body of arbitration rules that will apply once arbitral jurisdiction is invoked (or, in some cases, afford the claiming investor a choice of arbitration rules); most frequently, these are the ICSID or UNCITRAL Rules. Exceptionally, a few BITs contain express provisions regarding cost allocation, often in respect of jurisdiction issues, including the Netherlands/Poland BIT, the Australia/India BIT and the 2012 US Model BIT.

However, due to the predominance of their application in investor-state arbitration, the ICSID Convention and Rules as well as the UNCITRAL Rules are the primary focus of this discussion.

ICSID Convention and Rules

Two key features of the costs provisions contained in the ICSID Convention art.61(2), the ICSID Rules art.28 and the Additional Facility Rules art.58 are that: (i) these provisions contain no presumption that the successful party is entitled to recover any costs; and (ii)

there is a separation between arbitration costs and legal costs and the tribunal is granted discretion to decide how and by whom each is to be paid.

The ICSID Convention art.61(2) provides that:

> "In the case of arbitration proceedings the Tribunal shall, except as the parties otherwise agree, assess the expenses incurred by the parties in connection with the proceedings, and *shall decide how and by whom those expenses, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre shall be paid*. Such decision shall form part of the award."[18]

The ICSID Rules art.28 provides that:

> "(1) Without prejudice to the final decision on the payment of the cost of the proceeding, the Tribunal may, unless otherwise agreed by the parties, decide:
> (a) at any stage of the proceeding, the portion which each party shall pay, pursuant to Administrative and Financial Regulation 14, of the fees and expenses of the Tribunal and the charges for the use of the facilities of the Centre;
> (b) with respect to any part of the proceeding, that the related costs (as determined by the Secretary-General) *shall be borne entirely or in a particular share by one of the parties*."[19]

The ICSID Additional Facility Rules art.58 provides that:

> "(1) Unless the parties otherwise agree, the Tribunal shall decide how and by whom the fees and expenses of the members of the Tribunal, the expenses and charges of the Secretariat and the expenses incurred by the parties in connection with the proceeding shall be borne. The Tribunal may, to that end, call on the Secretariat and the parties to provide it with the information it needs in order to formulate the division of the cost of the proceeding between the parties.
> (2) The decision of the Tribunal pursuant to paragraph (1) of this Article shall form part of the award."

There plainly is no presumption in favour of a successful party recovering its costs in ICSID arbitration. The ICSID Convention offers no substantive criteria to determine or even to guide a tribunal's decision on cost allocation, and this is generally left entirely in the discretion of the tribunal. Neither the ICSID Arbitration Rules nor the ICSID Additional Facility Rules offer guidance on the cost allocation question beyond what is found in the Convention itself.

The ICSID Convention and Rules all list separately the "expenses incurred by the parties in connection with the proceedings (i.e. legal costs) from the costs of the tribunal and the institution (arbitration costs). Whilst the tribunal retains the same complete discretion in respect of each, the language of the costs allocation provisions certainly leave it open to the tribunal to make a different decision in respect of each category.

ICSID Travaux reveal no presumption

The *travaux préparatoires* to the ICSID Convention further reveal that the drafters expressly elected to omit any presumption that the successful party should be entitled to recover its costs. Indeed almost every draft prior to the final version contained an express presumption to the opposite effect: that each party would bear its own costs,[20] subject only to a "fairness

[18] ICSID Convention art.61(2) (emphasis added).
[19] Emphasis added.
[20] According to A. R. Parra, *History of ICSID Convention* (Oxford: Oxford University Press, 2012), one draft version of the cost-allocation provision read as follows: "Except as otherwise agreed by the parties, each party to

corrective" to be applied where a party behaved in an abusive, dilatory or otherwise inappropriate manner.[21]

In particular, the preceding drafts provided:

(i) "Except as otherwise agreed by the parties, *each party to a[n] ... arbitration proceeding shall bear its own expenses and the fees and expenses of the Center and of ... the Arbitral Tribunal... shall be divided between and borne equally by the parties*; provided, however, that if a … Tribunal determines that *a party has instituted the proceedings frivolously or in bad faith*, it may assess any part or all of such fees and expenses against that party."[22]

(ii) "Except as the parties shall otherwise agree,

> *each party to a[n] ... arbitration proceeding shall bear its own expenses in connection therewith*, and charges payable for the use of the facilities of the Center, as well as the fees and expenses of members of the… Tribunal… shall be borne equally by the parties; provided, however, that if a … Tribunal determines that a party *has instituted proceedings frivolously or in bad faith*, it may assess any part or all of such expenses, fees and charges against that party."[23]

(iii) "The charges payable for the use of the facilities of the Center, as well as the fees and expenses of members of the … arbitral Tribunal, *shall be borne equally by the parties*, and each party respectively shall bear such other expenses as it may incur in connection with any … arbitration proceedings; provided, however, that if in any arbitration proceeding the Tribunal determines that a party has instituted proceedings *or has conducted its defense frivolously or in bad faith*, it may assess any part or all of such charges, fees and expenses against such party."[24]

It is instructive to observe how these early drafts evolved into the final language in the Rules and Convention. Tellingly, it was a lengthy, negotiated process to move from each party bearing its own costs (particularly legal costs) except where bad faith, to the final position of leaving the matter to the discretion of the tribunal to determine costs on a case by case basis. A recurring theme throughout the negotiations was that the equal bearing of costs was consistent with the character of the ICSID regime of dispute resolution.

At the First Preliminary Draft Convention in September 1963, the Austrian delegate Mr Franz Oellerer commented that:

> "in court procedures the court costs were generally assessed against the unsuccessful party, and that in some countries even lawyers' fees of the successful party were charged to the unsuccessful party, [but (he thought)] *it was more customary in arbitration—which was not only a less formal but also a friendlier proceeding—to provide for equal sharing of costs* … . While it was, of course, possible for the parties to agree on a different division of costs, it seemed that, as a general rule, equal division of costs was most consonant with the whole character of the Draft."[25]

a[n] … arbitration proceeding shall bear its own expenses and the fees and expenses of the Center and of … the Arbitral Tribunal … shall be divided between and borne equally by the parties; provided, however, that if a … Tribunal determines that a party has instituted the proceedings frivolously or in bad faith, it may assess any part or all of such fees and expenses against that party" (*Working Paper (Doc.6)*, dated March 13, 1962, art.VII, s.1).

[21] For example, one of the earlier drafts of the ICSID Convention provided that "if a … Tribunal determines that a party has instituted the proceedings frivolously or in bad faith, it may assess any part or all of such fees and expenses against that party" (*Working Paper (Doc.6)*, dated March 13, 1962, art.VII, s.1).

[22] *Working Paper (Doc.6)*, dated March 13, 1962, art.VII, s.1 (emphasis added).

[23] Preliminary Draft (Doc.24), art.VI, s.1 (emphasis added).

[24] First Draft (Doc.43), dated September 11, 1964, arts 62 and 64(3) (emphasis added).

[25] SID/63-16 (September 20, 1963), Memorandum of the discussion by the Executive Directors, September 10, 1963, *Discussion of the First Preliminary Draft Convention*, p.176 at [11] (emphasis added).

The Chairman of the Working Group Mr Aron Broches replied that "solicitors' fees and, where necessary, travel costs *would be part of a party's own expenses* which under Section 1 of Article VI would be borne by that party alone".[26]

At the Consultative Meeting of Legal Experts in December 1963, Mr Broches further pointed out that "Section 1 of Article VI dealt with frivolous claims by providing that an arbitral tribunal, instead of applying the normal rule of apportionment of costs, could assess the costs of proceedings against the claimant".[27] The Chairman explained that "the clause [allowing the tribunal to assess the costs of proceedings against a party which has brought a frivolous or vexatious claim] had been introduced to allay the fears expressed in certain quarters that States might be exposed to unreasonable claims".[28]

The Chairman later clarified that tribunals would be empowered in such cases to award costs to include the expenses of the opposing party.[29] The delegate from Guinea suggested that "a distinction should be made between frivolous claims and claims brought in bad faith" with all costs to be assessed against the claimant party in the latter case alone.[30] The Chairman responded that the "term 'frivolous' in English was a very strong one and bordered on 'irresponsible'. The distinction between bad faith and 'irresponsibility' might be so fine that it was better left to be determined by the Tribunal."[31]

At the Consultative Meeting of Legal Experts in early February 1964, various delegates, including a number from Latin America, argued in favour of a broader ability to recover costs, extending beyond the limited scope of bad faith. In response to those various remarks, the Chairman surmised that "[i]n any case the aim would be to find the system most likely to appeal to the majority of the countries that would wish to accede to the Convention".[32]

In mid-February 1964, the Austrian delegate first suggested that the draft Convention "might well go beyond [international practice] and introduce the principle current in many national systems that the losing party would be required to pay all expenses" and that such approach "might somewhat lessen the risk of actions being brought unnecessarily".[33] At the same time, the German delegate expressed concerns that the current draft might "discourage many small and medium-sized enterprises whose investment in foreign countries it was particularly important to encourage from submitting disputes to the Center" and suggested that "some form of appeal in the matter of the assessment of costs" be added.[34]

In December 1964, Brazil suggested that "the charges payable for the use of the Centre, as well as the fees and expenses of the members of the Conciliation Commission or Arbitral Tribunal, [should] be borne by the unsuccessful party to the dispute, but that each party respectively [should] bear such other expenses as it may incur in connection with any conciliation or arbitration proceedings," and that the rest of art.62 of the ICSID Convention "be eliminated".[35] In discussions by the Legal Committee at that time, the Chairman noted Austria's proposal that "the losing party should always bear the entire costs and expenses

[26] SID/63-16 (September 20, 1963), Memorandum of the discussion by the Executive Directors, September 10, 1963, *Discussion of the First Preliminary Draft Convention*, p.177 at [13]–[14] (emphasis added).

[27] Consultative Meeting of Legal Experts (Addis Ababa, December 16–20, 1963), *Summary Record of Proceedings*, pp.257–258.

[28] Consultative Meeting of Legal Experts (Addis Ababa, December 16–20, 1963), *Summary Record of Proceedings*, p.277.

[29] Consultative Meeting of Legal Experts (Santiago, Chile, February 3–7, 1964), *Summary Record of Proceedings* dated June 12, 1964, p.351.

[30] Consultative Meeting of Legal Experts (Addis Ababa, December 16–20, 1963), *Summary Record of Proceedings*, p.278.

[31] Consultative Meeting of Legal Experts (Addis Ababa, December 16–20, 1963), *Summary Record of Proceedings*, p.278.

[32] Consultative Meeting of Legal Experts (Santiago, Chile, February 3–7, 1964), *Summary Record of Proceedings* dated June 12, 1964, p.353.

[33] Consultative Meeting of Legal Experts (Geneva, February 17–22, 1964), *Summary Record of Proceedings* dated June 1, 1964, p.436.

[34] Consultative Meeting of Legal Experts (Geneva, February 17–22, 1964), *Summary Record of Proceedings* dated June 1, 1964, pp.436–437.

[35] SID/LC/54 (December 9, 1964), *Legal Committee on Settlement of Investment Disputes, Comments by Mr da Cunha (Brazil) on Certain Articles of Ch.IV*, p.819.

with the understanding that there might be an apportionment of the costs in the case where a party only lost its case partially". The Chairman also noted the Brazilian proposal.[36] The Japanese delegate stated that "in the case of arbitration the responsibility for the costs of the proceedings should be determined by the Tribunal whereas the cost of each party should be borne by themselves, and that a conciliation commission also be permitted to assess costs against a party acting frivolously or in bad faith".[37] Meanwhile, Austria amended its proposal "to allow the Tribunal to make the decision with respect to costs as it saw fit *except where the parties had otherwise agreed*". The majority of delegates adopted this Austrian proposal.[38]

As evidenced by the above excerpts of successive versions of art.61(2), this provision evolved significantly throughout the discussions amongst the delegates of the Contracting Parties.[39] The Working Paper, the Preliminary Draft and the First Draft embodied the principle that each party should bear its own expenses and ICSID charges whereas the fees and expenses of the tribunal should be borne equally by the parties. Only where a tribunal determined that a claimant had instituted the proceedings frivolously or in bad faith could it award any of these costs against that party.[40] Later drafts clarified that the sanction for bad faith would apply not only to a claimant but also to a respondent.[41]

It was only the subsequent stages of the debate that led to proposals that would permit an unsuccessful party to bear the costs absent bad faith or frivolous conduct,[42] while alternative proposals favoured a flexible system which afforded discretion to the tribunal in light of the circumstances of each case.[43] In apparent endorsement of the Austrian proposal, a large majority of delegates voted in favour of the provision which allows the tribunal discretion on the assessment of costs absent any contrary agreement of the parties.[44]

UNCITRAL Rules

Similar features in respect of costs allocation exist in the UNCITRAL Rules. The 1976 UNCITRAL Rules are largely aligned with the ICSID Rules and Convention, insofar as there is no presumption in favour of the successful party recovering its legal costs (although there is such a presumption in respect of the arbitration costs). In the 2010 UNCITRAL Rules, such presumption was extended to all costs. In both sets of UNCITRAL Rules, there is a clear separation between arbitration costs and legal costs; tribunals retain the discretion to decide how and by whom each is to be paid.

The 1976 UNCITRAL Rules art.40 expressly carves out "the costs of legal representation" as follows:

> "1. Except as provided in paragraph 2, the costs of arbitration shall in principle be borne by the unsuccessful party. However, 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.
>
> 2. With respect to the costs of legal representation and assistance referred to in article 38, paragraph (e), the arbitral tribunal, taking into account the

[36] SID/LC/SR/20 dated January 5, 1965, *Summary Proceedings of the Legal Committee Meeting* on December 10, 1964, p.873.
[37] SID/LC/SR/20 dated January 5, 1965, *Summary Proceedings of the Legal Committee Meeting* on December 10, 1964, p.873.
[38] SID/LC/SR/20 dated January 5, 1965, *Summary Proceedings of the Legal Committee Meeting* on December 10, 1964, p.873 (emphasis added).
[39] See, e.g., S. W. Schill, "Arbitration Risk and Effective Compliance—Cost-Shifting in Investment Treaty Arbitration" (2006) 7 J. World Investment & Trade 653, 659.
[40] Parra, *History of ICSID Convention* (2012), p.274.
[41] Parra, *History of ICSID Convention* (2012), p.274.
[42] Parra, *History of ICSID Convention* (2012), p.276.
[43] Schreuer et al., *The ICSID Convention: A Commentary*, 2nd edn (2009), p.1228.
[44] Schreuer et al., *The ICSID Convention: A Commentary*, 2nd edn (2009), p.1228.

circumstances of the case, shall be free to determine which party shall bear such costs or may apportion such costs between the parties if it determines that apportionment is reasonable."

The "carve-out" in respect of "costs of legal representation and assistance" was eliminated in the 2010 UNCITRAL Rules. Article 42 now provides that:

> "1. The *costs of the arbitration shall in principle be borne by the unsuccessful party or parties*. However, 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."[45]

Some commentators suggest that this amendment had little substantive effect to the Rules in respect of costs allocation.[46] However, given that the amendment has subsequently been used as a basis for argument in favour of similar reform to the ICSID regime,[47] its effect may be more significant than anticipated or intended. On its face at least, the change appears to be a dramatic departure from the existing principle that there is no presumption in investor-state arbitration that the successful party is entitled to recover its legal costs (as opposed to arbitration costs). The legal costs are of course vastly more significant in terms of quantum and there is real risk of material disparity, based on the parties' available means and ability and preparedness to invest in the proceedings.

It is plain that the new language of the UNCITRAL Rules is not "substantially similar" to or simply maintaining the effect of the original provision of the 1976 Rules. The 1976 version of the UNCITRAL Rules contains a more detailed provision which dictates that recovery of the parties' costs and expenses is more difficult than recovery of the arbitration costs. In the 1976 UNCITRAL Rules, the drafters expressly elected not to establish a particular cost allocation rule as to the parties' costs of legal representation, leaving apportionment, if any, entirely to the discretion of the tribunal.

UNCITRAL travaux

As with the ICSID Convention and Rules, it is instructive to revisit the *travaux préparatoires* for both the 1976 UNCITRAL Rules and the 2010 UNCITRAL Rules in respect of the rules governing costs allocation.

1976 UNCITRAL Rules *travaux*

During the preparation of the 1976 UNCITRAL Rules, the discussion of art.38(e), which defines the legal costs of the successful party, was closely intertwined with the discussion of the language that became the art.40(2) "carve-out" of those costs. In particular, there was debate as to whether art.38(e) should include the language "if the arbitrators deem that legal assistance was necessary under the circumstances of the case". At the same time, there

[45] Emphasis added.

[46] Caron suggests that "Article 42 is substantially similar to corresponding Article 40 of the 1976 UNCITRAL Rules in purpose and function", and that the "amalgamation of standards" that it operates "has little substantive effect on the operation of Article 42"; "[t]hough the general standard proceeds from the principle that the costs of arbitration shall be borne by the unsuccessful party (whereas the original standard on the costs of legal representation and assistance does not), both standards are sufficiently flexible so as to afford the arbitral tribunal wide discretion in apportioning legal costs in any reasonable manner it deems appropriate, in light of the circumstances of the case". See D. D. Caron and L. M. Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (Oxford: Oxford University Press, 2013), p.877.

[47] M. Hodgson, "Costs in Investment Treaty Arbitration: The Case for Reform" (2014) 11(1) T.D.M., available at *http://www.allenovery.com/SiteCollectionDocuments/Costs%20in%20Investment%20Treaty%20Arbitration.pdf* [Accessed October 6, 2014].

had been considerable support for the proposal to delete the words "if the arbitrators deem that legal assistance was necessary under the circumstances of the case".[48]

The French delegate noted that "the provisions in paragraph 1(e) of the existing draft were very flexible, and suggested that that text should be retained. The costs of a case could be very heavy, and there was no reason why the successful party should be forced to pay them".[49] The Chairman noted that "the question at issue was whether the costs referred to in subparagraph (e) were necessarily covered by the rule set out in paragraph 2 or whether a separate rule should be laid down for them".[50] The UK delegate noted that "subparagraph (e) was, in any event, not the appropriate place for the inclusion of any such rule. The purpose of that subparagraph was to define the costs in question and not to specify how they were to be apportioned".[51] The Committee ultimately decided to "retain paragraphs 1(a) to (e) as they appeared".[52]

In subsequent commentary, prior to the 2010 UNCITRAL Rules, Caron noted that:

> "[t]he *expenses associated with the prevailing party's legal representation* are included in the definition of the costs of arbitration with two qualifications: they must be 'claimed during the arbitral proceedings' and must be determined by the arbitral tribunal to be 'reasonable'… . In early drafts of the Rules, a third qualification limited compensation for legal costs to circumstances in which 'the arbitrators deem that legal assistance was necessary under the circumstances of the case.' This provision was deleted after being severely criticized on grounds that it unduly prejudiced the parties' right to choose their own legal representation. Other attempts to limit which legal expenses were included in the costs of arbitration also failed."[53]

During the 13th meeting of the UNCITRAL Committee on April 20, 1976, the delegates acknowledged that:

> "[T]here was a wide variety of practice in different countries as to whether parties bore their own costs of arbitration or whether the costs were borne by the unsuccessful party. It seemed, however, that no arbitration rules went so far as to provide that the unsuccessful party should pay compensation for legal assistance of the successful party without exception, as was the case in paragraph 1(e)."[54]

In the course of the same session, delegates further noted that "a question of principle was involved, since a poorer party might hesitate to seek justice if it feared that it might have to bear the costs of a richer party. They considered that *some provision should be*

[48] A/CN.9/SR.168, *Summary Record of the 168th Meeting* (April 14, 1975), pp.211–212, available at: *http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/A-CN.9-SR.168.pdf* [Accessed October 6, 2014].

[49] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.3 (para.6), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[50] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.4 (para.22), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[51] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.5 (para.23), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[52] UNCITRAL Committee (9th Session), *Summary Record of the 17th Meeting*, April 22, 1976, p.6 (para.38), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[53] D. D. Caron, Lee Caplan and Matti Pellonpää, *The UNCITRAL Arbitration Rules: A Commentary* (Oxford: Oxford University Press, 2006), pp.931–932 (emphasis added). Caron explains that the other proposals to limit recovery of legal costs included a proposal that "no compensation for legal assistance … be permitted" or that "compensation … be awarded only in the face of frivolous claims or dilatory tactics". See Caron et al. (2006), p.932 n.21 (emphasis added).

[54] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.2, available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

made for costs, but that it should be flexible: it was, for example, difficult to prove bad faith."[55]

The draft UNCITRAL costs provision was further considered in relation to the UN Economic Commission for Europe Arbitration Rules,[56] which imposed costs upon the unsuccessful party. However, the US delegate noted that those were "designed for a region where the predominant practice was that the unsuccessful party should in principle pay the costs of the legal assistance of the successful party; however *rules of international application* [including the ICC Rules and the ICSID Rules] … *adopted a neutral approach*."[57] The Chairman noted that "the majority preferred the secretariat version of paragraph 2 for all arbitration costs *except legal assistance fees*; for such fees, the majority preferred to leave the arbitrators free to decide if compensation should be made".[58] The discussion therefore turned upon "whether the costs referred to in subparagraph (e) [i.e. legal representation costs] were necessarily covered by the rule set out in paragraph 2 or whether a separate rule should be laid down for them".[59]

Ultimately, and consistent with the *travaux préparatoires*, the 1976 UNCITRAL Rules leave

> "the arbitral tribunal 'free to determine which party shall bear [legal] costs', without any presumption of compensation for the successful party, and may apportion such costs if such action is 'reasonable'. The only limitation on the arbitral tribunal's discretion is that it must in awarding costs consider 'the circumstances of the case'."

According to Caron:

> "The different standards for apportionment under the 1976 UNCITRAL Rules represented a compromise among the drafters. Early drafts of the 1976 UNCITRAL Rules contained a general principle of compensation that the unsuccessful party must bear the costs of arbitration, but that the arbitrators may apportion the costs between the parties if circumstances warrant. Some representatives criticized this approach, especially with respect to the costs of legal representation, as *inconsistent with state practice and prejudicial to less affluent parties*. They favored the rule that each party would bear its own expenses for legal representation, but that the arbitral tribunal was entitled to award such costs in appropriate cases. This view persuaded the drafters to incorporate two approaches to cost apportionment set forth, respectively, in Articles 40(1) and 40(2) of the 1976 UNCITRAL Rules."[60]

In practice arbitral tribunals have adopted a variety of approaches in applying the cost allocation provision of the 1976 UNCITRAL Rules. Some tribunals have "apportioned the costs of the arbitral tribunal equally and required the parties to bear their own legal costs, whereas others have applied the 'loser pays' principle".[61] Further, arbitral tribunals have

[55] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.3 (emphasis added), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[56] If we understand correctly, these are the UN ECE Arbitration Rules for certain categories of perishable agricultural products (emphasis added), available at: *http://www.unece.org/fileadmin/DAM/trade/agr/info/general_conditions/arbitration_rules.e.pdf* [Accessed October 15, 2014].

[57] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.4 (emphasis added), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[58] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.4 (emphasis added), available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[59] UNCITRAL Committee (9th Session), *Summary Record of the 13th Meeting*, April 20, 1976, A/CN.9/9/C.2/SR/13, p.4, available at: *http://www.uncitral.org/pdf/english/travaux/arbitration/1976Arbitration/ACN99C2SR13.pdf* [Accessed October 6, 2014].

[60] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), pp.867–868 (emphasis added).

[61] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.869.

understood the relationship between the successful party being entitled to recover its costs and the tribunal's general authority to order "reasonable" apportionment in different ways. Some arbitral tribunals have emphasised their "wide discretion" to allocate costs, sometimes without reference at all to the successful party being entitled to recover costs.[62] Such variety of approach is consistent with a wholly discretionary principle.

2010 UNCITRAL Rules *travaux*

In relation to the 2010 UNCITRAL Rules art.42, the drafters formulated a proposal "to amalgamate paragraphs (1) and (2), so as to make the apportionment of the costs of representation and assistance subject to the same principle as other costs currently governed by paragraph (1)". The drafters observed that the distinction between the different types of costs in paras 1 and 2 reflected different legal traditions and ultimately "it was considered by the Working Group that it was preferable to amalgamate both paragraphs as proposed".[63] On that basis, para.2 was deleted. At the time, it was suggested that a provision analogous to art.31(3) of the ICC Arbitration Rules be incorporated, but that proposal was rejected.[64] Further, the drafters added the words "or parties" to para.1 of the Article "to take account of multi-party arbitration".[65]

The amended art.42 of the 2010 Rules now applies, in accordance with art.1(3), subject to "any mandatory requirements with respect to cost apportionment established under the governing arbitration law".[66] Absent such restrictions, "the arbitral tribunal enjoys substantial flexibility under the Rules in apportioning the costs of arbitration".[67]

The 2010 Rules art.42(1) is now the source of the arbitral tribunal's power to apportion and allocate all costs of arbitration, including legal costs. The premise is that the unsuccessful party (or parties) shall bear all those costs "in principle". However, it remains possible for the tribunal to depart from this general principle and to allocate the costs in a different manner if it determines that such alternative allocation is "reasonable", taking into account the circumstances of the case.

When deciding whether it is reasonable to allocate the costs pursuant to art.42(1), the arbitral tribunal must "take into account the circumstances of the case". Neither the 2010 Rules nor the *travaux préparatoires* provide guidance on the meaning of this important requirement.[68] Some international tribunals applying the 1976 Rules have considered one or more of the following factors when deciding on the costs: the success of the parties on their claims, the conduct of the parties during the arbitral proceedings, the nature of the dispute and the nature of the dispute resolution mechanism.[69]

[62] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.866.

[63] A/CN.9/646, *UNCITRAL Report of the Working Group on Arbitration and Conciliation on the work of its 48th session* (New York, February 4–8, 2008) at [28]. Available at *http://www.uncitral.org/uncitral/en/commission/working_groups/2Arbitration.html* [Accessed October 15, 2014].

[64] During the discussions on revision of the UNCITRAL Rules, a proposal was made to replace the phrase "successful party" with a more neutral formulation, similar to the one contained in the 1998 ICC Arbitration Rules art.31(3) ("which of the parties shall bear [the costs]"), since "it might be easy in all instances to determine which party was to be considered the successful party." A/CN.9/646, *UNCITRAL Report of the Working Group on Arbitration and Conciliation on the work of its 48th session* (New York, February 4–8, 2008) at [29].

[65] A/CN.9/WG.II/WP.151/Add.1, *UNCITRAL Working Group II (Arbitration)*, 49th session (Vienna, September 15–19, 2008) at [40]. Available at *http://www.uncitral.org/uncitral/en/commission/working_groups/2Arbitration.html* [Accessed October 15, 2014].

[66] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.866.

[67] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.866.

[68] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.870.

[69] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.870.

Other arbitral institutional rules

Various other arbitral institutions administer investor-state arbitration pursuant to their institutional rules. Two of these are the Permanent Court of Arbitration and the Stockholm Chamber of Commerce.

The PCA Rules 2012 amalgamate and reconcile four prior sets of PCA procedural rules: the Optional Rules for Arbitrating Disputes between Two States (1992), the Optional Rules for Arbitrating Disputes between Two Parties of Which Only One is a State (1993), the Optional Rules for Arbitration Between International Organizations and States (1996) and the Optional Rules for Arbitration Between International Organizations and Private Parties (1996).

The 2012 Rules reflect a revision of these earlier rules "in light of the 2010 revisions to the UNCITRAL Arbitration Rules and the PCA's experience with its existing procedural rules and the 1976 UNCITRAL Arbitration Rules".[70] In fact, the Rules incorporate, in proceedings where only one party is a State, the 2010 UNCITRAL Rules art.42 as follows:

> "1. The costs of arbitration shall in principle be borne by the unsuccessful party or parties. However, 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.
> 2. The arbitral tribunal shall in the final award or, if it deems appropriate, in any other award, determine any amount that a party may have to pay to another party as a result of the decision on allocation of costs."[71]

The 1993 Optional Rules for Arbitrating Disputes between Two Parties of Which Only One is a State had previously, like the 1976 UNCITRAL Rules, separately provided that

> "[w]ith respect to the costs of *legal representation* … the arbitral tribunal, taking into account the circumstances of the case, shall be free to determine which party shall bear such costs or may apportion such costs between the parties if it determines that apportionment is reasonable."[72]

The 1993 Rules contained no presumption in respect of legal costs. However, in accordance with the 2010 UNCITRAL Rules, the 2012 PCA Rules removed that distinction and all costs now fall within the presumption that the successful party may recover these.

The 2010 SCC Rules provide that, unless otherwise agreed by the parties, the arbitral tribunal "shall, at the request of a party, apportion the Costs of the Arbitration between the parties, having regard to the outcome of the case and other relevant circumstances".[73] Unless the parties have agreed otherwise, the tribunal "may in the final award upon the request of a party, order one party to pay any reasonable costs incurred by another party, including costs for legal representation, having regard to the outcome of the case and other relevant circumstances".[74] The language "having regard to the outcome of the case" plainly does not constitute a presumption that the successful party is entitled to recover costs.

Public policy and costs allocation in investor-state arbitration

The amendments to the costs allocation provisions in the 2010 UNCITRAL Rules, and the corresponding change to the PCA Rules, signify a facial change at least in respect of the

[70] *New PCA Rules Adopted*, Permanent Court of Arbitration, available at *http://www.pca-cpa.org/shownews.asp?nws_id=347&pag_id=1261&ac=view* [Accessed October 6, 2014].

[71] Permanent Court of Arbitration Rules 2012 art.42. Available at *http://pca-cpa.org/shownews.asp?ac=view&pag_id=1261&searchkind=archive&nws_id=347* [Accessed October 6, 2014].

[72] Permanent Court of Arbitration 1993 Optional Rules for Arbitrating Disputes between Two Parties of Which Only One is a State at Art. 40 at [2] (emphasis added).

[73] 2010 Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce art.43(5).

[74] 2010 Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce art.44.

existence of a presumption of costs allocation in favour of the successful party, for arbitration costs *and* legal costs. However, the UNCITRAL Rules apply predominantly in international commercial arbitration, and to a far lesser extent in investor-state arbitration. And, whilst such amendment may indeed be descriptive of the prevailing practice in international commercial arbitration, it is less clear that it was intended to become *prescriptive* of practice in investor-state arbitration.

Commentators are divided in their views as to the potential, and indeed, desired prescriptive effect of the 2010 UNCITRAL Rules costs allocation changes in investor-state cases in particular. According to Caron, broadly speaking:

> "How arbitral tribunals apply the revised rule remains to be seen. Differing national practices may cause some arbitrators to resist applying the 'loser pays' principle to the apportionment of the legal costs. In addition, party expectations will likely influence how arbitrators use the broad *discretion afforded the arbitral tribunal* in the second sentence of Article 42(1). Because the single standard for apportionment contained in Article 42(1) is so flexible, a clear and consistent practice regarding cost recovery under the 2010 UNCITRAL Rules is unlikely to emerge for some time, if prior practice under the 1976 UNCITRAL Rules is any indication."[75]

Certainly a number of experts take the view that the change will have very little effect at all and that its purpose was largely to clarify the existing provision. A report by Jan Paulsson and Georgios Petrochilos suggests simply that the rationale behind the amendment was that:

> "[paragraph 2] fail[ed] to establish any meaningful distinction except a very vague indication that costs of legal representatives are less easily recoverable than other costs. Practice has shown that the discretion exercised by arbitral tribunals depends on the circumstances of each case; the current formulation adds confusion rather than predictability."[76]

Further, according to Webster, "[t]hat provision was deleted on the basis that those costs were already covered by the first section of the article".[77] Caron accepts that the new art.42 "represents a unification of the two distinct standards of apportionment previously found in the 1976 UNCITRAL Rules".[78] He nevertheless suggests that: "Article 42 is *substantially similar* to corresponding Article 40 of the 1976 UNCITRAL Rules *in purpose and function*", and that the "amalgamation of standards" that it operates "has little substantive effect on the operation of Article 42"; he comments:

> "[t]hough the general standard proceeds from the principle that the costs of arbitration shall be borne by the unsuccessful party (whereas the original standard on the costs of legal representation and assistance does not), *both standards are sufficiently flexible so as to afford the arbitral tribunal wide discretion in apportioning legal costs in any reasonable manner it deems appropriate, in light of the circumstances of the case*."[79]

However, Caron further acknowledges that investor-state arbitration is a "unique form of dispute resolution" and its unique nature may inform the tribunal in allocating costs. One current trend is to require the parties in investor-state arbitration to "divide the costs of the arbitral tribunal evenly and to bear their own costs of representation, save in cases of frivolous or bad faith claims"; one of the reasons for this approach is that investor-state

[75] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), pp.868–869.

[76] J. Paulsson and G. Petrochilos, *Revision of the UNCITRAL Arbitration Rules* (unpublished report, 2006), p.154 at [280] (emphasis added). Available at *http://www.uncitral.org/pdf/english/news/arbrules_report.pdf* [Accessed October 6, 2014].

[77] T. H. Webster, *Handbook of UNCITRAL Arbitration* (London: Sweet & Maxwell, 2010), p.590.

[78] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.867.

[79] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.877 (emphasis added).

arbitration "presents novel issues of international law, the resolution of which cannot be easily predicted".[80]

It is within this "unique form of dispute resolution" of investor-state arbitration that promotion of any prescriptive effect of the 2010 UNCITRAL Rules should be treated with caution. The only regime dedicated exclusively to investor-state arbitration is ICSID. It bears remembering that the ICSID Convention and Rules, designed exclusively for investor-state arbitration and not as a hybrid applied mostly in commercial cases, contain no presumption in favour of a successful party recovering its costs.

With the "unique" context of investor-state arbitration, Professor Wälde, in his separate opinion in *International Thunderbird Gaming Corp v United Mexican States*, drew a parallel between investor-state arbitration and GATT litigation. He highlighted the particular nature of international judicial review of government conduct, noting that:

> "The only concept under which this so far well-established rule has not been observed or a different treatment suggested is for '*manifestly spurious or unmeritorious' positions taken by the loser, unprofessional conduct and significant breach of good-faith in arbitration*. There are a good reasons [sic] for this approach which has so far been intuitively, but not yet explicitly appreciated by tribunals in thrall to the attitudes prevalent in commercial arbitration: *Investment arbitration is not a reciprocally agreed and structured method of dispute resolution. It is a unilateral right of investors—not mirrored by a reciprocal government right—to claim against alleged misconduct by governments under an investment treaty. It is in substance comparable at most to national and international judicial review of administrative conduct—rather than to the reciprocal 'contract' model of commercial arbitration*.
>
> …
>
> *Imposing the risk of government attorney costs on losing investors in effect undermines the very purpose of such treaties; it raises the litigation risk in factual situations which are as a rule ambiguous, confused and contradictory to a prohibitive level, in particularly* [sic] *for smaller companies for whom litigation risk is high and where a government enjoys significant superiority in terms of expertise, experience and resources available for defense* against NAFTA arbitration. … The highly unusual cost award thus casts a 'chill' over attempts by junior companies to rely on the NAFTA's investment protection regime and makes that recourse—very high-risk anyway—doubly prohibitive because of the now added cost risk. *In effect and in practice, it makes the recourse to independent justice for smaller companies prohibitive*."[81]

There are indeed public policy arguments against imposition of any presumption that the successful party should be entitled to recover legal costs in investor-state arbitration. For historic reasons of international comity it is a matter of practice and procedure (arguably a norm) that in public international law disputes between state parties—treaty or customary international law—each party generally meets its own costs except where the tribunal decides otherwise. Investor-state arbitration is a product of treaty, albeit invoked by a private party against a state. The extension to private parties of the right to obtain damages pursuant to the treaty terms does not automatically carry with it a right to the system of costs recovery that exists for actions between private parties in some (but not all) national litigation systems and increasingly exists in international commercial arbitration.

Moreover, even in those national litigation systems where a successful party is entitled to recover costs, often an action by a private individual against the state for review of a government decision, arising out of the administrative conduct of the state as opposed to

[80] Caron and Caplan, *The UNCITRAL Arbitration Rules: A Commentary*, 2nd edn (2013), p.874.

[81] *International Thunderbird Gaming Corp v United Mexican States*, Separate Opinion by Prof. Thomas Wälde (December 2005), at [139], [142] (emphasis added). Available at *http://www.italaw.com/sites/default/files/case-documents/ita0432.pdf* [Accessed October 6, 2014].

its commercial activities, will be an administrative or judicial review proceeding whereby the practice for the applicant party is *not* permitted to recover costs.

4. Conclusion

The increasingly prevalent practice in international commercial arbitration for the successful party presumptively to be entitled to recover its legal costs now appears to be codified under the 2010 UNCITRAL Rules, which will apply in some investor-state proceedings. The 2010 UNCITRAL Rules art.1(2) extends the scope of application of those Rules to arbitral proceedings conducted under arbitration agreements which were concluded after August 15, 2010 or, in the context of a bilateral investment treaty, to cases wherein the sovereign's offer to arbitrate is extended after August 15, 2010. Investor-state arbitral proceedings instituted pursuant to a BIT or Multilateral Investment Treaty (MIT) will ordinarily be subject to the version of the Rules in force at the time that the treaty was executed.[82]

It is not clear that the state parties to the various BITs and MITs which will apply those Rules, at the election of the investor, anticipated, intended or desire that outcome. The limited available empirical data in investor-state arbitration continues to demonstrate that no such presumption exists, at least in practice, in this "unique" field. Moreover, the *travaux* of the various rules and conventions indicate that such presumption was never intended to exist in this field of arbitration (despite its prevalence in commercial arbitration).

Under all applicable arbitration rules, tribunals do retain full discretion in allocating costs. A number of factors should be taken into account when rendering decisions on allocation of costs, including the relative success or failure of the parties,[83] the conduct of parties (including any vexatious or frivolous claims or conduct),[84] the novelty of the issues or the questions of law[85] and various considerations of equity.[86] Other relevant factors might include the public interest, any settlement endeavours of the parties and the parties' sources

[82] P. Binder, *Analytical Commentary to the UNCITRAL Arbitration Rules* (London: Sweet & Maxwell, 2013), p.30: The "motivation for including this exception to the presumption [that the Rules in force at the time of commencement of arbitral proceedings should apply] came from a concern that the introduction of the presumption could have led to the unintended retroactive application of the presumption where the arbitration agreement was formed by the claimant accepting an open offer to arbitrate extended by the respondent."

[83] *Mr Franck Charles Arif v Republic of Moldova*, ICSID Case No.ARB/11/23, Award April 8, 2013 at [631] (in the cost decision, the court ruled that "[i]n the current case, Claimant has been successful on the issue of jurisdiction, has established a breach by Respondent of the fair and equitable treatment standard of the France-Moldova BIT, and has established the right to restitution and damages. On the other hand, his claims for expropriation, denial of justice and moral damages have failed, as well as his claims of specific undertakings, discrimination and compensation"); *Swisslion DOO Skopje v The Former Yugoslav Republic of Macedonia*, ICSID Case No.ARB/09/16, Award July 6, 2012 at [355] (the court ruled in the cost decision that "the Claimant's major claims were rejected, thus necessarily leading to a dramatic reduction of the amount of damages that could be awarded").

[84] *Europe Cement Investment v Turkey*, ICSID Case No.ARB(AF)/07/2, Award August 13, 2009 (the court made the cost decision based on the claimant's bad faith and fraud); *Deutsche Bank v Sri Lanka*, ICSID Case No.ARB/09/2, Award October 31, 2012 (the court ruled the cost decision in the consideration of the respondent's bad faith and egregious breaches); *S.D. Myers v Canada*, UNCITRAL (NAFTA) Final Award on Costs December 30, 2002 at [45] ("The majority considers that conduct of an unsuccessful party which gives rise to liability is generally not relevant to the apportionment of costs. The purpose of an award of costs is not to punish a respondent for the conduct that made it liable to the claimant").

[85] *Robert Azfnian v Mexico*, ICSID Case No.ARB(AF)I97I2, Award November 1, 1999 at [126] (NAFTA "is a new and novel mechanism for the resolution of international investment disputes"); *Merrill & Ring Forestry v Canada*, UNCITRAL (NAFTA) Award, March 31, 2010 at [270] ("the Investor … raised questions of particular Interest for the Tribunal to consider both under NAFTA and international law"); *Orner Dede v Romania*, ICSID Case No.ARBI10/22, Award September 5, 2013 at [268] ("interpretation of the BIT was not obvious").

[86] *Fireman's Fund v Mexico*, ICSID Case No.ARB(AF)/02/1, Award July 17, 2006 at [221] ("it was a close one"); *EDF (Services) Ltd v Romania*, ICSID Case No.ARB/05/13, Dissent of Arthur Ravine Regarding Costs October 8, 2009 at [8] ("many of the close issues of fact and law in this case were crucial issues of fact and law"); *Berschader v The Russian Federation*, SCC Case No.080/2004, Award April 21, 2006 at [215] ("the obvious imbalance between the Parties in economic terms has to be taken into account"); *International Thunderbird v Mexico*, UNCITRAL Award January 26, 2006 at [214] (investor has limited financial resources, considerations of access to justice).

of financing.[87] When applying the 2010 UNCITRAL Rules, tribunals should at minimum be mindful that these factors all take on even more significance in investor-state arbitration.

In the future, states may consider addressing cost allocation provisions more frequently in their investment treaties to counter any unintended consequences of the 2010 UNCITRAL Rules.[88] Alternatively, parties may agree on a cost allocation in terms of reference or early procedural orders, or in the course of settlement.[89] In any event, all participants in the process should be aware of the historic approach to costs allocation in this "unique form of dispute resolution" and ensure that practices within it are not merged without due consideration into the more general practice of international commercial arbitration.

[87] *Kardassopoulos v Georgia*, ICSID Case No.ARB/05/18, Award March 3, 2010 at [691] ("The Tribunal knows of no principle why any such third party financing arrangement should be taken into consideration in determining the amount of recovery by the Claimants of their costs").

[88] *Eureko B.V. v Poland*, Partial Award and Dissenting Opinion, Ad Hoc Tribunal [UNCITRAL], IIC 98 (2005), August 19, 2005.

[89] *EVN AG v Former Yugoslav Republic of Macedonia*, ICSID Case No.ARB/09/10, Award September 2, 2011.