Awarding Costs in International Commercial Arbitration: an Overview

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I. INTRODUCTION

Resolving an international commercial dispute by arbitration is expensive for several reasons. High stakes and complex legal or technical questions at issue often lead to significant expenses for legal and other professional services. Moreover, since the parties have opted for a private means of dispute resolution, they will also have to pay the fees and expenses of the arbitrators. The administrative charge of any arbitral institution, the costs involved in hiring appropriate facilities for the hearings, as well as the fees for transcription services and any needed interpreters also must be met. As a result, the costs of international commercial arbitrations are regularly substantial, not only in absolute terms but also compared to the amount in dispute.[1]

Thus the question is: who will have to pay for what? Since commercial people want to know their likely financial exposure prior to investing their money, they often seek advice on how much the arbitration is going to cost them if they lose and whether they will recover their costs if they win. A quick answer to this question may be: 'generally, the loser pays,' but this statement does little to dispel the *flou artistique* which can sometimes be observed in arbitral practice on costs. There is indeed an arbitral precedent to support nearly any approach a tribunal may wish to apply to its cost decision. Even cost awards rendered under the same arbitration rules sometimes vary fundamentally without any apparent reason. The bottom line is that it is often impossible to predict with any satisfactory degree of certainty how the costs will be awarded.

The uncertainties mainly stem from two sources: first, not all arbitrators follow the same principles in order to determine *which party* should pay (all or a part of) the costs of arbitration. Second, arbitrators may take different views on *which costs* incurred by a party are reimbursable. Before focussing

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1 According to W. Laurence Craig/William W. Park/Jan Paulsson, *International Chamber of Commerce Arbitration* (2000), at p. 395: 'awards on costs in excess of $1 million are unremarkable in the biggest cases.' See also Eric A. Schwartz, *The ICC Arbitral Process, Part IV: The Costs of ICC Arbitrations*, in ICC Ct. Bull., Vol. 4 (1993) p. 8.

on these two issues, *i.e.* the allocation of costs and the determination of recoverable costs, it is worth first setting up the general framework regarding costs.

II. THE GENERAL CONCEPT OF COSTS – WORK IN PROGRESS?

A. Procedural Costs and Parties' Costs

In arbitration, costs are usually categorized into two groups: procedural costs and parties' costs; together they constitute the costs of arbitration[2]. The procedural costs include the fees and expenses of the arbitrators as well as the fees and expenses of any arbitral institution or of experts appointed by the arbitral tribunal.[3] The parties' costs are those incurred by a party for the preparation and presentation of its case before the arbitral tribunal.[4]

B. Sources of Confusion

A leading textbook notes that 'no general practice as to the treatment of costs in international commercial arbitrations could be discerned.'[5] The patchy approach in international arbitration parallels the various national costs systems in litigation, and the different theories regarding costs.

1. Two Opposing Principles

Most fundamentally, two diametrically opposed conceptions prevail about what should be the basic principle: (i) the rule of '*costs follow the event*' or '*loser-pays rule*' states, in essence, that the losing party is to compensate the winner for its costs, whereas (ii) the so-called *American rule* provides that each party bears its own legal costs regardless of the outcome of the dispute. The former approach can claim to be 'almost universally recognised'[6] and is embraced by both common and civil law jurisdictions. Nonetheless, the latter concept is not only applied in the United States, but also in Japan, the People's Republic of China, Indonesia and the Philippines.[7] Either approach,

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2 See, *e.g.*, Article 38 Swiss Rules. The terminology is, however, not uniform. Some arbitration rules use the term 'costs of the' confined to what is described here as 'procedural costs'.

3 The determination of the procedural costs (and of the fees of the arbitrators, in particular) is not treated in this paper.

4 Michael Bühler/Sigvard Jarvin, *The Arbitration Rules of the International Chamber of Commerce*, in Practitioner's Handbook on International Arbitration (2002), *ad* Article 31 ICC Rules, note 41.

5 Alan Redfern/Martin Hunter, *Law and Practice of International Commercial Arbitration* (1999), at p. 406.

6 Draft Principles and Rules of Transnational Civil Procedures, UNIDROIT 2002, at p. 63.

7 *Id.*

however, may claim to be just: the 'loser-pays rule' insofar as it provides that the prevailing party who has proven the righteousness of its position should not suffer any financial harm; the *American rule* insofar as it claims that the losing party may have had good and justified reasons for pressing a strong but ultimately unsuccessful claim or defence.

2. Costs Claims: a Matter of Procedural or Substantive Law?

Most countries consider the decision on costs and fees to be a matter of procedural law.[8] However, the key rationale for awarding costs to the successful party is that 'a claimant who is forced to resort to court action to enforce his claim against a reluctant debtor is entitled to recover the full value of the claim and should not be expected to be satisfied with a lesser amount because of the necessity of suing'.[9] This is, in essence, a perception of costs akin to consequential damages: from the prevailing claimant's perspective, it is the respondent's substantive wrong that caused his legal expenses. Given this situation, it seems obvious that a claimant will look to the substantive law for an alternative cause of action to be compensated for its costs if the procedural law does not give redress. For instance, a party may try to claim the expenses it had to pay for defending a court action brought by its opponent in disregard of the arbitration agreement as damages arising from the substantive breach of the arbitration agreement.[10]

The 'full value' argument, however, does not give ready support for awarding costs to a prevailing respondent. Here, the entitlement to costs must be linked to the legal proceedings themselves, since the mere fact of bringing a losing claim does not, unless an action can be considered vexatious, constitute an actionable wrong. From the respondent's perspective, it is thus regularly the procedural law only which can provide a basis for cost recovery. An important motive for awarding costs to the prevailing respondent is that a losing claimant's cost liability serves as safeguard against unnecessary or unjust litigation. In arbitration, however, this policy argument

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8 John Gotanda, *Awarding Costs and Attorneys' Fees in International Commercial Arbitrations*, (1999) 21 Michigan J. Int'l L. 2, p. 16.

9 See Werner Pfennigstorf, *The European Experience with Attorney Fee Shifting*, in (1984) 47 Law & Contemp. Probs., at p. 66.

10 See Jane Wessel/Sherri Noth Cohen, *In Tune with Mantovani: The 'Novel' Case of Damages for Breach of an Arbitration Agreement*, (2001) Int.A.L.R., p. 65 *et seq.*; and Otto Sandrock, *Malicious parallel suits in foreign jurisdictions – A paper-tiger gets teeth*, Stockholm Arbitration Report 2003:1, p. 219 *et seq.*

may not have the same force since 'here, the only people who may be made respondents are those who have willingly signed up for it. '[11]

In an international context, this 'oscillating' legal nature of costs causes particular difficulties: Does it become necessary to decide which law prevails if the substantive law is more permissive than the procedural law? If not, can it be right that the claimant, but not the respondent, may recover certain costs as damages?

3. The Idiosyncrasies of the National Cost Systems

Added to the aforementioned difficulties are the idiosyncrasies of the various national civil procedure rules. Although the rule that 'costs follow the event' has a longstanding tradition in Europe, a comparative analysis of cost practices in European civil procedure rules reveals a picture of 'confusing variety and complexity'.[12] Not only is the 'costs follow the event' rule subject to a wide range of different qualifications, but even the understanding of who 'won' the case may not be the same depending on which national civil procedure is applied.[13] Regarding the determination of recoverable costs, and in particular with respect to lawyers' fees, the national regulations are complex. The rules and guidelines are burdened with policy considerations peculiar to each country, and they are often the fruit of compromises which can only be understood against the historical background and in light of the specific structure of the national judicial system and the legal profession.[14]

C. The 'Compromise' in International Arbitration

The variety of approaches regarding the treatment of costs was replicated in arbitration since, in this respect, the national arbitral laws and practices often copied from court practice. Confronted with this situation, the drafters of the UNCITRAL Model Law on International Commercial Arbitration concluded that 'questions regarding the fees and costs of arbitration [are] not an appropriate matter to be dealt with in the model law.'[15] Nor did the drafters (and 'revisers' respectively) of the most widely used 'truly international' arbitration rules, namely the ICC Rules and the UNCITRAL Rules, consider

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11 Michael O'Reilly, *Rethinking costs in commercial arbitration*, (2003) 69 Arbitration - Journal of the Chartered Institute of Arbitrators, at p. 122.

12 Werner Pfennigstorf, *op. cit.*, at p. 66.

13 See section IV.B. hereunder.

14 In France, for instance, attorneys' fees are not usually recoverable; see, however, Art. 700 of the New Code of Civil Procedure.

15 Report of the Working Group on International Contract Practices, UN Doc. A/CN.9/216 (1986), at p. 99.

the time to be ripe for laying down clear guidelines for the treatment of costs. Rather, they left the issue to the widest discretion of the arbitrators.[16] This compromise comes, however, at the price of predictability, since in a dispute resolution mechanism in which the parties, their lawyers and the arbitrators may all come from different legal backgrounds, different expectations and practices as to costs are bound to collide.

D. The Applicable Law as to Costs

In international commercial arbitration, tribunals 'routinely award costs and attorneys' fees, usually without discussing questions of applicable law.'[17] The short explanation is that there is often much discretion but little 'law' on the issue. Nonetheless, the arbitral 'matrix" of (procedural) provisions created by the parties' express agreement, their agreement by reference to arbitration rules, if any, and the *lex arbitri* of the seat of arbitration also determines the cost issues. Although the applicable arbitration law usually will not restrict the parties' autonomy with regard to costs issues,[18] arbitration agreements, rarely deal with the issue of costs.[19] Primarily, one will thus have to consult the arbitration rules. Indeed, any of the most frequently used arbitration rules addresses the issue of costs. Yet, the comprehensiveness of the solutions adopted in the various rules as well as the scope of discretion conferred therein on the arbitrators vary quite significantly.[20]

1. The Scope of the Lex Arbitri as to Costs

Absent a reference to arbitration rules, the default provisions of the *lex arbitri* are of particular relevance. However, arbitration acts may not deal with costs: for instance, neither Chapter XII of the Swiss Private International Law nor Book IV of the French New Code of Civil Procedure contain a provision on costs. Now, if both the arbitration agreement and the act are silent on the matter, and no arbitration rules were agreed upon by the parties, where should the arbitrator look for the law to apply? It is sometimes argued that in this case, the arbitral tribunal is bound to follow the cost rules applicable to

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16 See below sections IV.A and V.A.

17 John Gotanda, *op. cit.*, at p. 18.

18 See, however, section 60 of the English Arbitration Act of 1996 which provides: '[a]n agreement which has the effect that a party is to pay the whole or part of the costs of the arbitration in any events is only valid if made after the dispute in question has arisen'. According to section 4(1) and Schedule 1 of the act, this provision is mandatory.

19 The standard arbitration clauses as suggested by the different institutions do not address costs issues.

20 Some rules start from the presumption that costs follow the event, others leave the decision to the unfettered discretion of the arbitrators. Compare, for instance, Art. 31 ICC Rules and Art. 28 LCIA Rules.

judicial proceedings at the place of arbitration.[21] However, in a transnational dispute, it would often be inappropriate for arbitrators to do so, since the national regulations and practices are as diverse as they are complex (and thus neither the parties nor the arbitrators may be familiar with them). Nowadays, the view that the rules of state court procedure are applicable as 'stopgap' measures for arbitral proceedings has largely been abandoned.[22] Actually, modern arbitration laws do not consider the parties' choice of the arbitral seat to be an implicit choice of that country's procedural law (other than specific provisions for arbitral proceedings), but rather give the arbitrators the subsidiary power to determine the procedure.[23] Absent any specific provision in the arbitration law or an agreement of the parties, arbitrators thus have an unfettered discretion in making their decision on costs as a result of their power to determine the arbitral procedure.

If the parties have adopted a certain set of arbitration rules, it must be assumed that such reference includes the provisions therein relating to the determination and allocation of costs.[24] In this case, the scope of the arbitrators' discretion is defined by the cost provisions in the agreed arbitration rules since the *lex arbitri* endorses the parties' contractual cost regime. Thus, it is on that basis that the tribunal will render its cost award.

In principle, the situation is the same when the applicable arbitration law has a set of default rules regarding costs. However, problems may arise when the parties have opted for arbitration rules which deal with costs in a rather general fashion (and in essence point to the arbitrator's complete discretion) while the *lex arbitri* provides for detailed provisions which are to be applied 'unless otherwise agreed'. For instance, does Article 31(3) ICC Rules supersede the detailed 'cost code' of the English Arbitration Act of 1996 ('1996 Act')? Mustill/Boyd deny that 'a block contracting out, replaced by nothing concrete' is permitted,[25] and other authors expressly emphasize that Article 31(3) ICC Rules is not specific enough to free the tribunal from complying with Sections 61(2) and 63 of the 1996 Act.[26]

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21 This was, for instance, the prevailing view in England.

22 See Philippe Pinsolle/Richard Kreindler, *Les limites du rôle de la volonté des parties dans la conduite de l'instance arbitrale*, 2003/1, Revue de l'arbitrage, p. 41 et seq.

23 See, *e.g.*, Art. 182(2) PIL and Article 1494 NCPC.

24 Markus Wirth, Art. 189 PIL, in *International Arbitration in Switzerland*, note 55.

25 Lord Mustill/Stewart Boyd, *Commercial Arbitration,* 2001 Companion Volume to the Second Edition (2001), at p. 39 et seq.

26 Bruce Harris/ Rowan Planterose/ Jonathan Tecks, *The Arbitration Act 1996 – A Commentary* (2000), at p. 276 and 285.

From an international perspective, an applicability of Sections 61 (2) and 63 of the 1996 Act in ICC proceedings in England would be particularly fastidious if, as some leading textbooks seem to suggest,[27] these provisions are a mere restatement of the law as it stood before. Indeed, England has been for a long time the prime example for requiring the arbitrators to process to a 'taxation" as done in court.[28] They were 'bound to act judicially' and 'must apply the same principles when dealing with costs as are applied in the High Court'.[29] Yet, the principles on costs as developed in judicial case law and set down in the Civil Procedure Rules are, from an international perspective, rather eccentric and so complicated that, if applicable to international arbitrations in England, they are likely to be a pitfall to both a foreign party and a non-English arbitrator.[30] According to *Fence Gate v NEL Construction Ltd*, however,

> 'it is no longer helpful to ask whether an arbitrator has acted 'judicially' or has acted in an equivalent way as a judge would have acted in a similar situation when reaching a judicially determined costs decision.'[31]

Accordingly, an arbitrator sitting in England is no longer required to follow the litigation practices when exercising his discretion under the 1996 Act, as long as it is exercised on some rational and justifiable basis (and explained accordingly in the award).[32]

The conclusions to be drawn from the above are threefold: first, the cost rules followed in national courts at the place of arbitration are not binding on the tribunal (unless so agreed by the parties).[33] Second, both the *lex arbitri* and the applicable arbitration rules will be confined, if at all, to the

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27 Lord Mustill/Stewart Boyd, *op. cit.*, at p. 413.

28 See J. Gillis Wetter/Charl Priem, *Costs and their Allocation in International Commercial Arbitrations* (1991) 2 Am. Rev. Int'l. Arb. 251, p. 254 *et seq.*

29 D. Mark Cato, *Arbitration Practice and Procedure: Interlocutory and Hearing Problems* (1997), at p. 413.

30 See, for instance, D. Mark Cato, *op. cit*, p. 534, on how to tax the parties' costs in English arbitration.

31 82 Con. L.R. 41, per Thornton J, para. 33.

32 See, in particular, Hew R. Dundas, *Recent Developments Regarding Costs in Litigation: Are they Applicable in Arbitration?*, (2003) 69 *Arbitration - Journal of the Chartered Institute of Arbitrators*, p.90 et seq.

33 See, *e.g.*, ICC Case No. 8786 (1997), 20 ASA Bulletin 1 (2002), at p. 68; and *Brega Oil Marketing Company* v *Techint Compagnia et Tecnica Internazionale SpA, Tribunal Cantonal du Canton de Vaud* (16 February 1993), 13 ASA Bulletin 1 (1995), p. 57 *et seq.* The cantonal court found that an ICC arbitral tribunal in an arbitration in Switzerland is not bound to apply the cost provisions as applicable before state court.

basic principles as to the treatment of costs. Third, arbitrators will have a wide discretion when deciding cost matters.

2. Discretion as a 'Backdoor" for National Practices

When exercising this discretion, arbitral tribunals sometimes take into consideration the laws and practices as to costs in effect at the *locus arbitri*[34] or in the parties' jurisdictions;[35] presumably on the basis that, although not directly applicable, they give an indication of the parties' expectations. However, in doing so, arbitrators should keep in mind that 'the practice of national court in following its own rules in relation to awarding costs hardly seems to provide compelling guidelines for the way in which an international tribunal should exercise the discretion granted to it.'[36] This solution may be adequate insofar as the rules applied by the tribunal are common to both parties' legal system. For the rest, there seems to be little justification to look to the rules of state court procedure at the *locus arbitri* for guidance merely because the seat of the arbitral proceedings has been agreed or otherwise determined to be in that jurisdiction.[37]

Finally, national practices may have a more subliminal impact on the treatment of costs: arbitrators are not always immune to the influence of their own domestic civil procedure or national arbitral practice and, in reality, tend to follow their approach.[38]

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[34] See, *e.g.*, ICC Case No. 6345 (1991), ICC Ct. Bull., Vol.4 (1993), p.45; ICC Case No. 6282 (1992), ICC Ct. Bull., Vol.4 (1993), p. 42; ICC Case No. 6962, 19 (1994) Y.B. Com. Arb., p. 193.

[35] See, *e.g.*, ICC Case No. 6345 (1991), ICC Ct. Bull., Vol.4 (1993), p.45; ICC Case No. 5946 (1990), 16 (1991) Y.B. Com. Arb., p. 118; Final Award of 4 May 1999 in *Himpurna California Energy Ltd* v *PT. (Persero) Perusahaan Listruik Negara*, 25 (2000) Y.B. Com. Arb. 13, p. 106; see also Final Award of 16 October 1999 in *Himpurna California Energy Ltd* v *Republic of Indonesia*, 25 (2000) Y.B. Com. Arb., p. 213 et seq.

[36] Alan Redfern/Martin Hunter, *op. cit.*, at p. 410.

[37] See the observations by Eric M. Runesson/Mikael Swahn on the Award in SCC Case 129/2000 (2002), Stockholm Arbitration Report, 2003:1, p. 135.

[38] See Murray L. Smith, *Costs in International Commercial Arbitration*, (2001) 56 Disp. Res. J. 30; Michael Bühler, *Costs in ICC Arbitration: A Practitioner's View*, (1992) 3 Am. Rev. Int'l. Arb. 116., p. 143.

III. THE AUTHORITY TO AWARD COSTS

Many national arbitration laws[39] and all of the most widely used arbitration rules[40] expressly confer on the arbitrators the authority to decide the costs of arbitration as between the parties.[41] Other national laws assume that such powers are inherent in the arbitrators' mandate to resolve a dispute.[42] Actually, an arbitral tribunal is usually not only authorised to decide on the costs as between the parties, but it also is obliged to do so.[43] Accordingly, the arbitrators' jurisdiction to decide on costs is normally indisputable, but – as it will be shown – there are exceptions.

A. The American Exception

In the United States, the American rule also applies to arbitration.[44] This rule is understood to mean that a tribunal in an arbitration in the U.S. has the power to award party representation costs to a prevailing party 'only if the parties' contract, a specific statute or the arbitration rules so allow'.[45] Accordingly, the courts have regularly vacated arbitral cost awards for want of authority to award legal fees.[46] Consequently, the arbitration agreement becomes of central importance since courts will uphold a cost award for attorneys' fees if the arbitration clause expressly contemplates a 'fee-shifting'. Moreover, several courts have given a wide scope of application to the contractual approach.[47] In particular, it was found that the parties'

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39 See, *e.g.*, section 61(1) 1996 Act and section 1057 of the German Code of Civil Procedure.

40 See, *e.g.*, Article 38 UNCITRAL Rules, Article 31(3) ICC Rules, Art. 38 Swiss Rules, Art. 28 LCIA Rules.

41 In institutional arbitration, the determination of the amount of the procedural costs is regularly reserved to the institution. While the decision as to which party will have to bear which part of the procedural costs remains on the tribunal, it is not competent to fix itself the amount of such costs.

42 This is the case in Switzerland and France.

43 Note, however, section 63 (4) 1996 Act.

44 W.H. Howard, *Awarding Attorney's Fees in Connection with Arbitration*, (1998) 60 A.L.R. 5th 669, (with a compilation of the principal cases from 1974-98); Gary B. Born, *International Commercial Arbitration* (2001), p. 913.

45 Thomas H. Oehmke, *Commercial Arbitration* (1990 and Suppl. 1994), 123:01.

46 See the cases cited by W.H. Howard, *op. cit.*, § 5. There are, however, some courts which have taken the position that a tribunal has the implied powers to award such costs unless foreclosed by contract: *Porush v. Lemire,* 6 F.Supp.2d 185 (1998, E.D.N.Y); *PaineWebber Inc.* v. *Bybyk,* 81 F.3d. 1193 (1996, 2nd Cir.).

47 Some courts held that when both parties had sought an award of attorneys' fees in their favour during the arbitral proceedings, the awarding of party costs was contemplated by the parties to be within the scope of the arbitration agreement: e.g., *Ludgate Insurance Company Ltd.* v. *Banco de Seguros del Estado,* 2003 WL 443584 (2003, S.D.N.Y.). Moreover, it was held that arbitration clauses drafted with a wide scope – *e.g.* 'any and all disputes . . . shall be determined by arbitration' – are to be read as covering the powers to decide on legal costs, since any ambiguities as to the scope of the arbitration agreement are to be resolved in favour of arbitration: *e.g.*, *ACE Capital Overseasa Ltd.* v. *Cent. United Life Insurance,* 307 F.3d 133 (2002, 2nd Cir.

reference to a set of arbitration rules allowing the tribunal to assess attorneys' fees suffices to confer such authority on the tribunal.[48] Moreover, one court held that since 'the law on the powers of arbitrators to award attorneys' fees to prevailing parties in spite of the general 'American rule' prohibition is not well-settled', an award granting such fees cannot fall afoul of the 'manifest disregard" standard.[49] Nevertheless, from a practical viewpoint, parties intending to enter into a contract providing for arbitration in the U.S. should specifically address the issue of attorneys' fees in the arbitration clause.[50] Finally, it should be emphasized that the American rule is not considered to be part of U.S. public policy.[51]

B. Jurisdiction to Award Costs Without Jurisdiction to Decide the Merits?

Whether a tribunal which declines jurisdiction remains competent to determine the costs as between the parties is controversial. The position rejecting such authority is based on the argument that a tribunal's jurisdiction to decide on costs can only result from the agreement to arbitrate, and that arbitrators do not, in this respect, enjoy any residual decision-making powers separate from jurisdiction on the merits (as courts do).[52] In a sense, the problem is an appendix to the debate on *Kompetenz-Kompetenz*. Presumably, a provision in the *lex arbitri* providing that the tribunal shall allocate the costs of the arbitration unless otherwise agreed is specific enough to vest a tribunal with such residual jurisdiction, at least *vis-à-vis* the claimant who unsuccessfully relied on an agreement to arbitrate.[53] Arbitration rules may expressly provide that the tribunal remains competent to award costs against the claimant.[54] With the same view, the reference to 'the merits of the case' was omitted in Article 31(3) ICC Rules.[55] However, since arbitration rules

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48 *E.g., Thomas,* 921 SW2d 847 (1996, Tex App); *McKee* v. *Hendrix,* 816 So.2d 30 (2001, Ala.Civ.App.); contra: *Prudential-Bache Sec., Inc.* v. *Depew* 814 F.Supp. 1081 (1993, MD Fl.).

49 *Ludgate,* 2003 WL 443584. See also Hans Smit, *Attorneys' fees in Arbitration in New York,* (1999) 10 Am. Rev. Int'l Arb. 95, p. 96.

50 See W.H. Howard, *op. cit.*, § 2.c.

51 Gary B. Born, *op. cit.*, p. 913. In *August AASMA* v. *American Steamship Owners* (238 F.Supp.2d 918, 922) it was held that neither Article V(1)(c) nor Article V(2)(b) of the New York Convention provide a bar to the recognition of a cost award rendered in an English arbitration and granting the prevailing party its legal costs on the basis of the default provisions of the 1996 Act. Since costs were 'not merely arbitrarily assigned', the award could not be said 'to violate most basic notions of morality and justice of the American justice system'.

52 See Hans W. Fasching, *Der Kostenersatzanspruch des Beklagten bei Unzuständigkeitausspruch des Schiedsgerichtes*, in *Festschrift für Walter J. Habscheid* (1989), p. 93 et seq.

53 In this sense: Bundesgerichtshof, Decision of 6 June 2002, Schieds VZ 2003/1, p. 40.

54 See Article 62(3) of the Rules of the Netherlands Arbitration Institute.

55 See Yves Derains/Eric A. Schwartz, *A Guide to the New ICC Rules of Arbitration* (1998), p. 339 et seq.

only apply by virtue of the agreement to arbitrate (which is lacking here), it is questionable whether they can actually help to circumvent the problem.

Prudent arbitrators will, if the plea of lack of jurisdiction is raised, seek to obtain the parties' express written consent that the tribunal may assess costs even if it should decline jurisdiction on the merits.[56] In ICC cases, this is regularly achieved by way of carefully drafted terms of reference.[57] Despite the above-mentioned controversy, arbitrators have normally considered themselves to be competent to award costs to a party which requested that the other party's claim be dismissed for lack of jurisdiction with costs.[58] Indeed, no apparent injustice is done to the latter party since it wrongfully initiated the arbitration and thus caused the other to incur costs. Moreover, if the respondent had not taken part in the proceedings, the claimant would have had to bear the costs anyway (and would already have paid the entire advance on costs). When confronted with the controversy, national courts can be expected to be slow to interfere with the tribunal's decision.[59]

IV. ALLOCATION OF COSTS

A. Costs Follow the Event – a Universal Starting Point in International Arbitration?

Some recently published arbitral decisions hold that 'according to general principles' or 'in accordance with basic procedural principles followed in arbitration', the costs of arbitration should be borne by the party which loses the arbitration.[60] Similarly, several practitioners have observed an emerging trend for arbitral tribunals to order the losing party to bear both the

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56 See J. Gillis Wetter/Charl Priem, *op. cit.*, p. 326.

57 *E.g.*, ICC Case No. 10574 (2001), (2001) 16 Mealy's Int'l. Arb. Rep. 62-63.

58 See, *e.g.*, the awards in ICC No. Case 5896 (1992), ICC Ct. Bull., Vol.4 (1993), p.37; ICC Case No. 3383, 7 (1982) Y.B. Com. Arb. p.123; and SCC Case 129/2000 (2002), Stockholm Arbitration Report, 2003:1, at p.127.

59 See *Austin John Montague* v *Commonwealth Development Corporation* (27 June 2000), Supreme Court of Queensland, Court of Appeal Division, in 26 (2001) Y.B. Com. Arb. at p. 744-748. See also in this context the decision dated 3 April 2003 of the Swiss Federal Court, DTF 128 III 191 in which the Court upheld an award assessing the procedural costs against an 'inexistent' claimant: 'Le Tribunal arbitral était compétent pour examiner l'argument de la défenderesse selon lequel la demanderesse n'avait pas la capacité d'être partie ni celle d'ester en justice. (...) S'il admettait cet argument, il ne pouvait pas statuer sur les conclusions au fond prises par la partie inexistante. En revanche, rien ne lui interdisait de mettre une partie des frais à la charge de l'entité qui l'avait mis en œuvre en présentant faussement comme une personne morale existante.'

60 See the Awards in ICC Case No. 8486 (1996), 24 (1999) Y.B. Com. Arb. at p. 171; ICC Case No. 7645 (1995), 26 (2001) Y.B. Com. Arb. at p. 151; ICC Case No. 8528 (1996), (25) Y.B. Com. Arb. at p. 352.

procedural and the legal costs incurred by the other party.[61] Indeed, some newer arbitration laws expressly provide that the tribunal shall award the costs of arbitration on the principle that costs follow the event unless the circumstances of the case warrant a departure from such rule.[62] Several arbitral rules adopt the same approach.[63] Interestingly, Principle 25.1 of the Draft Principles of Transnational Civil Procedure of the Joint Working Group of the International Institute for the Unification of Private Law ('UNIDROIT') and the American Law Institute also states that 'the winning party ordinarily should be awarded all or a substantial portion of its reasonable costs.' Costs include court filing fees, fees paid to officials such as court stenographers, expenses such as expert-witness fees, and lawyers' fees.[64]

Having said that, other factors cast doubt on the idea that the loser-pays rule has emerged as the universally recognised principle for the treatment of costs in international commercial arbitration. First, the most widely used 'truly international' arbitration rules do not require a tribunal to award costs to the successful party. The ICC Rules are silent on cost allocation inasmuch as Article 31(3) does not offer any criteria for the arbitrators' decision on which party should bear the costs of arbitration. In the absence of any guidelines in the ICC Rules, the matter is left to the absolute discretion of the arbitrators.[65] While adopting the principle that costs follow the event with regard to the procedural costs in Article 40(1), the UNCITRAL Rules[66] omit any reference to the outcome of the proceedings with regard to the legal costs. Rather, Article 40(2) expressly states that the tribunal is free to decide on such costs as it sees fit. This would suggest that, as far as legal costs are concerned, the outcome on the merits does not serve as the prevailing yardstick.[67] Second, the loser-pays rule cannot be called the

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61 *E.g.*, Julian Lew/Loukas Mistelis/Stefan Kröll, *Comparative International Commercial Arbitration* (2003), note 24-82.

62 *E.g.*, section 61(2) 1996 Act; section 1057(1) German Civil Code of Procedure.

63 Art. 38.4 LCIA Rules; section 35.2 DIS Rules; Art. 40(2) and 41 SCC Rules; Art. 61(2) NAI Rules.

64 Draft Principles of Transnational Civil Procedures, UNIDROIT 2004, Study LXXVI – Doc. 11.

65 Similarly, Art. 61(2) ICSID Convention; Art. 26 CEPANI Rules, Art. 19 Vienna Rules.

66 See the analogous Art. 40(1) and (2) Swiss Rules.

67 In *Sylvania Technical Sys. Inc.* v. *Government of the Islamic Republic of Iran*, (1985) 8 Iran-U.S. C.T.R. Rep. 329, the tribunal observed: 'Whereas according to these provisions costs other than for legal representation and assistance shall as a rule be borne by the unsuccessful party, the Rules are not so clear with regard to costs for legal representation and assistance. The above-quoted provision of Art. 38, paragraph 1(c), mandating the Tribunal to fix the legal costs of the successful party, seems to indicate an intention that such costs shall also be borne by the unsuccessful party. Article 40, paragraph 2, however, clearly leaves broader discretion to the Tribunal to determine who shall bear such costs. In addition, the seemingly mandatory provision of Article 38, paragraph 1(c), is to a large extent modified by the fact that the Tribunal shall fix such costs '*only* to the extent' that it deems them reasonable (emphasis added). While this does not create a presumption in favour of the exemption

traditional approach in international arbitration. In interstate arbitrations, for instance, it has been customary that each party bears half of the procedural costs as well as its own legal costs. In mixed arbitration, too, the loser-pays rule seems to be the exception rather than the rule. ICSID tribunals (and NAFTA tribunals under the Additional Facility) have not established a uniform practice as regards the award of costs and expenses.[68] The loser-pays rule was followed in a minority of cases only.[69] In most cases, the tribunals simply ordered each party to bear half of the procedural costs and left the parties' costs where they fell without giving any specific reasons.[70] Significantly, in all but one case where the claimant failed entirely, the defending government was not awarded any costs. *Waste Management Inc.* v. *Mexico*[71] seems to be the only case where the private party was ordered to bear the procedural costs because it lost its case (nonetheless, legal costs were not allocated).

There is no recent empirical data to corroborate that in international commercial arbitration a party will normally recoup most of its costs if it prevails (without a contractual basis to that effect, or in its absence, a presumption to that effect in the *lex arbitri*). However, a study[72] undertaken by the ICC of the final awards rendered in ICC arbitrations between 1989 and 1991 showed that out of 48 cases in which the claimant clearly prevailed, in 39 cases, or 81%, the tribunal ordered the respondent to bear all or most of the procedural fees, while only in 24 cases, or 50%, the claimant was also awarded its legal costs. In 36 cases in which the claimant obtained substantially less than half of the amount claimed or less than the amount awarded to the respondent, the claimant had to bear the procedural costs in 12 cases, but all or part of the respondent's legal costs in only nine cases. In an earlier analysis of 26 published ICC awards, it was found that out of 16 cases in which one party was the decisive winner, it was awarded costs in 13 decisions (81%).[73] However, only in six of these cases the published sections of the cost awards confirm that also legal costs were awarded.

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from the stated rule, it indicates that the test of 'reasonableness' as required here should be applied in a rather cautious manner.'

68 This was expressly stated, for instance, in *Compania de Aguas del Aconquija S.A.* v. *Argentine,* 16 ICSID Rev.–FILJ, para. 94.

69 See the cases referred to by Christoph Schreuer, *The ICSID Convention: A Commentary* (2001)., p. 1225-1227.

70 See the cases cited in Christoph Schreuer, *op. cit.*, p. 1229, note 41.

71 121 I.L.R. 30 (2002).

72 Cited in Eric A. Schwartz, *op. cit.*, ICC Ct. Bull., Vol.4 (1993) 8, p. 21 et seq.

73 Lester Nurick, *Costs in International Arbitrations* (1992) 7 ICSID Rev.-FILJ 57.

Both surveys thus corroborate a pronounced tendency to consider the outcome on the merits as the determining factor for the allocation of the procedural costs. With regard to party costs, the picture is, however, less clear. There are few indications as to the motives for a different allocation of the two cost categories.[74] Yet, it is difficult to see why the procedural costs and the parties' costs should be treated differently, unless the arbitrators considered the allocation of legal costs inappropriate absent recklessness or bad faith on behalf of the losing party.[75]

B. Who is the Winner?

If the outcome of the dispute is the most significant factor in relation to cost allocation, then the arbitral tribunal has to ask itself 'who was the successful party?' or 'what is the event?' Again, the arbitrators' answer might be quite different depending on their legal background.

In countries such as Austria, Germany, Sweden and Switzerland, the civil procedure rules require a proportional allocation reflecting each party's relative success of the claims and defences. The same approach is prevalent in the arbitration practice of those countries.[76] [77]The rationale is that if a claimant is awarded less than claimed, this difference constitutes a success from the respondent's perspective. Accordingly, costs are allocated *inter partes* on a sliding scale proportionate to the amount in dispute.[78] This means that a claimant must assess the strength of its claim and its amount as

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74 See Markus Wirth, *op. cit.*, note 58, who holds that 'a diverging allocation can be justified if the losing party by its behaviour caused the opposing party, but not the arbitral tribunal, considerably greater expense or vice versa.'

75 According to Michael Bühler/Sigvard Jarvin, *op. cit.*, p. 301, n. 74, 'the rationale for such approach may be that in an international arbitration it should be the sole responsibility of each party how it presents and defends its case'; W. Laurence Craig/William W. Park/Jan Paulsson, *op. cit.*, p. 395, suggest that this is 'perhaps in order to avoid insult to injury'.

76 Eric A. Schwartz, *op. cit.*, p. 21; see also DFT 116 II 373 in which the Swiss Federal Tribunal considered this approach to be 'self-evident'.

77 An arbitral tribunal in Switzerland is, however, not bound to allocate the costs on the basis of the relative success of each parts, *C. S.r.l.* v *L.S. S.A.*, Swiss Federal Tribunal, decision of 9 June 1998, cons. 3.b)dd), in 16 ASA Bulletin 3/1998, p. 660. Similarly, as regards Germany, the Oberlandesgericht Stuttgart: 'Die Kostenentscheidung, die trotz weitgehendem Obsiegen die gesamten Kosten auf die Antraggegnerin überbürdet, verstößt nicht gegen den deutschen Ordre public', decision dated 15 March 2001, in IHR 5-2001, at p. 212.

78 For instance, if the claimant (or counterclaimant) makes a claim for 120, and judgement is given to the claimant in the full amount, the respondent is to pay all of the claimant's costs (and vice versa if the claim is fully denied). If only 60 is awarded, then each party's relative degree of success is 50%. Therefore, each party has to compensate the other for half of the latter's costs, or the success rates are simply set off against each other (i.e. each party bears its own costs). Similarly, if the claimant obtains a judgment for 90, the degree of success is 75% for the claimant and 25% for the respondent; thus the costs are awarded in a proportion of 3 to 1 or the respondent has to compensate the claimant for half of its costs.

realistically as possible in order not to be penalised on costs. Similarly, the respondent is encouraged to make an offer as near as possible to the 'real" value of the claim in order to avoid costs.[79]

In England, costs are usually awarded to the 'net winner" and this approach is also applied in arbitration:

> 'If a claimant recovers a monetary award, he is normally to be regarded as successful since he had to bring the arbitration in order to recover the sum in question. The 'event' is the recovery of money. It is normally no ground for depriving the claimant of his costs that the amount recovered is less than that claimed unless the recovery is so small that it can be regarded as nominal or derisory.'[80]

It is evident that this approach may lead to the opposite result of an allocation according to the relative success of the parties. Yet, the 'net winner' principle is intrinsically linked with the English practice of 'sealed offers'.[81] In essence, this means that the respondent may cap its cost risk by making a 'sealed' settlement offer in the course of the arbitration. Such offer will not be revealed to the tribunal until the substantive issue have been decided. Only then is it 'opened': if the arbitrator finds that the claimant would have recovered the same or more by accepting the offer, the claimant is to recover his costs up to the time when the offer could have been accepted, but is to pay the respondent's costs incurred for the period after that time. The advantage of this practice is that it puts the respondent under considerable pressure to submit an offer at an early stage. By contrast, there is little incentive for the claimant not to 'reasonably' inflate its claim in the beginning, since he will recover all his costs if he 'beats' the offer even by a small margin only.

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79 However, if in the above example the respondent had made an offer for 90 which the claimant rejected, and the court then awarded 90 to the claimant, the respondent would nevertheless have to compensate the claimant for half of its costs, unless the court takes the rejected offer into consideration.

80 Chartered Institute of Arbitrators, *Guidelines for Arbitrators on Making Orders Relating to Costs of Arbitration*, para. 16. See also *Channel Island Ferries Ltd* v. *Cenargo Navigation Ltd* (1994), TLR 5 April 1994, per Phillips J.: 'It was an error in principle in the exercise of an arbitrator's discretion as to costs not to award a claimant the entirety of his costs solely on the ground that he had recovered significantly less than claimed. [Counsel] suggested that where a claimant had recovered significantly less than claimed, the practice of not awarding the entirety of his costs, on the ground that he had been only partially successful, had become prevalent among arbitrators. If there were such a practice, it was desirable that it should stop.'

81 Regarding the practice of 'sealed offers' or 'Calderbank letters' see, for instance, D. Mark Cato, *op. cit.*, p. 448 et seq.

The English approach may not to be easily applied in an international setting. Without the counterbalance of 'sealed offers', the 'net winner' principle puts the parties into an unequal position. Taking settlement offers into consideration when assessing costs normally requires a division of the decision on the merits and on costs.[82] Although most arbitration laws and arbitral rules would allow the arbitrators to decide the merits in a preliminary award and then fix the costs in the final award, the general practice in international arbitration is to decide both issues together.[83] Especially in the ICC regime, with its scrutiny process of any award rendered, such a split may be overly burdensome unless the amount of costs at stake justifies a separate final award on costs. Moreover, it has to be taken into consideration that under many institutional systems the fees of the arbitrators and the administrative charge of the institution is computed on the basis of the amount in dispute. Here, the losing respondent would actually have to pay for the claimant's exaggeration of the claim if he is ordered to bear all procedural costs. Furthermore parties from civil law jurisdictions will not be accustomed with the 'sealed offers' practice. In this case, a tribunal intending to adopt the English approach should thus inform the parties at the very outset of the proceedings that they may submit such offers, and that the tribunal intends to take them into consideration when deciding on costs.

In many cases neither of the aforementioned approaches will be appropriate without adaptation to the specific circumstances. When a case involves several claims, it may not be adequate to simply compare the total figure of money claimed and awarded.[84] At the same time, it may become impractical to identify the different 'events" when several claims and counterclaims are raised or different legal grounds are invoked. Still, there are further difficulties. In ICC Case No. 5029, the tribunal pointed out:

> 'Ideally, one would compare exactly how much money was spent on each claim and then apportion each amount depending upon the success enjoyed by the parties for each claim. At least two problems emerge from any attempt to follow the ideal route. First, it is impossible for the Arbitral Tribunal to determine from the submissions of the parties the costs spent on each claim with any

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82 Unless the offer is made as an 'open' offer. However, parties normally want to avoid that the arbitrators are influenced by such offer when considering the substance of the case.

83 Julian Lew/Loukas Mistelis/Stefan Kröll, *op. cit.*, note 24-86.

84 Regarding the English practice, see Tony Bingham, *Taking Issue with Events: A Commentary about Awarding Costs*, (2003) 69 Arbitration - Journal of the Chartered Institute of Arbitrators, p. 122 *et seq.*

> precision. Second, 'success per claim', measured with mathematical exactitude, does not necessarily reflect the nature and complexities of a given claim, or whether the time and money spent, was at the end of the day, justified.'[85]

Hence, an arbitral tribunal may look beyond the relation between the amounts claimed and awarded in respect of a given claim. For instance, a claimant may have prevailed on the issue of liability, which had constituted a central aspect of the proceedings, but then failed to establish damages as claimed. Here, a tribunal has reason to treat the two issues separately, including the costs involved in each 'sub-proceeding'.[86] All in all, an allocation of costs based on the outcome of the case rarely can or should be a strict arithmetic exercise. Although arbitrators should not use 'too broad a brush', pointillism is of no use either. Little, if anything, is gained if the allocation and determination of the costs degenerates into a costly mini-arbitration. As a consequence, in cases where no party substantially prevailed, arbitrators regularly order each party to bear half of the procedural costs and its own costs.[87]

C. Circumstances Resulting in an Allocation other than Costs Follow the Event

In those arbitration laws and rules, which expressly provide that costs follow the event, this principle is by no means made absolute. It is invariably subject to the broad exception that the arbitrator, in the exercise of his discretion, may depart from the presumption if the circumstances of the case so require.[88]

Conversely, in ICC arbitrations, the tribunals' considerations regarding costs regularly first refer to the outcome on the merits, although no presumption in favour of the successful party is made in the ICC Rules. In ICC Case No. 11670[89], the tribunal held:

> 'Le Règlement d'arbitrage ne contient ni règles ni critères au sujet de la décision que doit prendre le Tribunal arbitral. Il laisse la décision à la discrétion complète de l'arbitre. Néanmoins, l'issue de l'arbitrage

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85 ICC Case No. 5029 (1991), ICC Ct. Bull., Vol.4 (1993), p. 32.
86 See the cases cited in footnote 91 hereunder.
87 See Eric A. Schwartz, *op. cit.*, p. 22.
88 *E.g.*, Section 61(2) 1996 Act and Article 28.4 LCIA Rules.
89 ICC Case No. 11670 is reprinted in this issue of the ASA Bulletin, p. 333.

joue un rôle prédominant dans l'exercice de cette discrétion par l'arbitre. Une partie qui perd son action, en principe, est condamnée aux frais de l'arbitrage. Cependant, d'autres critères peuvent également être retenus [...].'

The following synopsis gives an overview regarding the various rationales applied by ICC tribunals when allocating costs differently than based on the outcome.

Issue-based allocation: ICC tribunals regularly take into consideration that an ultimately unsuccessful party prevailed on preliminary issues, particularly if a procedural defence was dismissed[90] or if the claimant succeeded on liability, but lost on quantum[91]. This approach is, however, rather a refinement of than an exception to the loser-pays rule.

Procedural misconduct or dilatory tactics: ICC tribunals have regularly awarded costs against or refused, partially or entirely, to award costs to a prevailing party as a sanction against dilatory, obstructive or otherwise improper procedural conduct.[92]

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90 In ICC Case No. 8786 (1997), 13 ASA Bulletin 1 (1995), p. 57 *et seq.*, the prevailing respondent was awarded only 80% of its legal costs since it had applied for an interim award on security which the tribunal dismissed. In ICC Case No. 5901 (1992), ICC Ct. Bull., Vol.4 (1993), p. 40, the successful respondent was awarded only a part of its reasonable legal costs due to the fact that, *inter alia*, it was only partially successful on its 'initial procedural defences'. In ICC Case No. 6914 (1992), ICC Ct. Bull., Vol.4 (1993), p. 48, the unsuccessful claimant had to bear only three quarters of the procedural costs and of the respondent's reasonable legal costs, because, *inter alia*, the respondent's unfounded objection of the claimant's capacity to act. See also ICC Case No. 5587 (1992), ICC Ct. Bull., Vol.4 (1993), p. 35.

91 See, *e.g.*, ICC Case No. 5587 (1992), ICC Ct. Bull., Vol.4 (1993), p. 35: 'Claimant has only succeeded in its claim to an extent of approximately 1/6 and failed accordingly to an extent of 5/6. (...) This arithmetical outcome, however, cannot be followed to assess Claimant's responsibility for the costs. Indeed, the difficulty of the proceedings consisted mainly in establishing the principle of Defendant's liability, not so much in assessing the damage.' Accordingly, the tribunal found that both parties should bear their own costs and half of the procedural costs. See also ICC Cases No. 6042 (1991) and 6673 (1992), both in ICC Ct. Bull., Vol. 4 (1993), p. 41/47.

92 *E.g.*, ICC Case 8486 (1996), (1999) 24 Y.B. Com. Arb., p.172: 'Nonetheless, the costs of the arbitration shall be borne totally by the defendant. (...) According to good faith, the parties to an international arbitration must in particular facilitate the proceedings and abstain from all delaying tactics (...). The behaviour of the defendant during the entire proceedings did not comply with theses requirements in any way.'; ICC Case No. 7453 (1994), (1997) 22 Y.B. Com. Arb., p. 124; ICC Case 6955 (1993), (1999) 24 Y.B. Com. Arb., p.139; ICC Case 7661 (1995), (1997) 22 Y.B. Com. Arb., p. 163; ICC Case No. 5901 (1992), ICC Ct. Bull., Vol. 4 (1993), p. 39 ('it is somewhat abusive on [Respondent's] part to try to bar Claimant's claim by reason of *res judicata* after having refused to let the Terms of Reference in the first proceedings be amended, thus [not] allowing the Arbitral Tribunal in initial proceedings to determine those very claims').

Immoral or corrupt agreement: Some tribunals have found that if a contractual claim was denied because the underlying agreement was *contra bonos mores* and therefore void, it would not be just if the prevailing party, which had co-operated in the conclusion and performance of such agreement, could recover its costs.[93]

Inflated claim: In an ICC arbitration in England, the tribunal held that 'the amounts claimed by the Claimants were in our view unjustifiably inflated, resulting in unnecessary high fees having to be deposited with the ICC. This exaggeration had little effect on the amount of work which had to be done, which was considerable, but we think that the Claimants should not recover from the Respondent the full amount of the advance on fees which they paid to the ICC.'[94]

Burden of proof and difficulties to prove: In the exercise of their discretion, arbitrators sometimes take into consideration that a claimant mainly lost due to understandable difficulties in providing sufficient evidence[95] or due to the fact that it was not without considerable hesitation that the tribunal preferred the evidence of one party's expert witness over that of the other.[96]

Bona fide dispute and fairness: In several decisions, ICC tribunals used their discretion to moderate the effect of a strict 'loser-pays" approach. In ICC Case No. 8332, the tribunal held that since the dispute arose out of the unclear terms of the parties' agreement, each party should 'bear a share of the responsibility for this uncertainty and the resulting costs', even though the claimant prevailed on all material issues.[97] In ICC Case No. 6728, the arbitrators did not grant costs to the prevailing respondent because the claim was 'far from being reckless' and partly arose out of a confusion created by the respondent's conduct.[98] Similarly, in ICC Case No. 6955, the tribunal refused to award costs to the prevailing claimant because, *inter alia*, the factual basis of its case was brought to the respondent's attention only upon the commencement of the arbitral proceedings.[99] In another case, costs were

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93 ICC Case No. 6248 (1990), (1994) 19 Y.B. Com. Arb. 124; ICC Case No. 5717 (1989), cited in Lester Nurick, *op. cit.*, p. 74.
94 ICC Case No. 5726 (1992), ICC Ct. Bull., Vol.4 (1993), p. 35.
95 ICC Case No. 6673 (1992), ICC Ct. Bull., Vol.4 (1993), p. 47.
96 ICC Case No. 6042 (1991), ICC Ct. Bull., Vol.4 (1993), p. 41.
97 ICC Case No. 8332 (1996, unpublished).
98 ICC Case No. 6728 (1992), ICC Ct. Bull., Vol.4 (1993), p. 47.
99 ICC Case No. 6955 (1993), (1999) 24 Y.B. Com. Arb. p. 139.

denied because 'only the strength of the contract has caused this success, which is no reflection of either party's behaviour'.[100]

D. Loser Pays: Reparation and Dissuasion

The higher the costs for bringing or defending a claim, the more important it becomes for a party to assess its cost exposure. This legitimate need for predictability calls for a rule establishing the principle for the allocation of costs. Moreover, the uncertainty as to how costs are allocated adds a possible source of disagreement between the parties what and this is likely to reduce the chances of settlement.[101] It is argued here that in international commercial arbitration, arbitrators should, as a rule, allocate costs in a manner which reflects the parties' relative success and failure in the arbitration, unless special circumstances warrant an exception or the parties otherwise agree.[102]

From a successful claimant's perspective, the cost of bringing a claim before an arbitral tribunal is the cost of making the opponent comply with its contractual (or quasi-contractual) undertakings. Consequently, awarding costs to the successful claimant is in line with the remedial doctrines.[103] In addition, this approach has a strong foundation in economic theory: by imposing the costs of wrongful conduct, the loser-pays rule provides economically efficient deterrence for such conduct and furthers compliance with contractual obligations.[104] From a successful respondent's perspective, it is suggested that the equity of awarding costs stems from the fact that a respondent confronted with an arbitral claim is forced either to settle or to take part in the proceedings, and thus to incur costs. A further compelling argument for awarding costs to successful respondents comes from the deterrent effect of the loser-pays rule on frivolous or exaggerated claims which have been brought for their nuisance value or for strategic reasons only. The risk of having to compensate the respondent for its costs, if the claim is unsuccessful, causes claimants to raise the 'expected value threshold below which they will not file their claims'.[105] The notion that a loser-pays rule reduces the frequency of speculative claims as well as the overall

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100 ICC Case No. 7761 (1995), (1997) 22 Y.B. Com. Arb. 163.

101 See Thomas D. Rowe, *Predicting the Effects of Attorney Fee Shifting* (1984) 47 Law & Contemp. Probs., p. 154 *et seq.*, in particular note 71.

102 See, for instance, section 1057(1) German Civil Code of Procedure, Art. 28.4 LCIA Rules and Art. 56 and 57 ZCC Rules (1989).

103 See Thomas D. Rowe, *The Legal Theory of Attorney Fee Shifting: A Critical Overview* (1982) Duke L. J. 658.

104 *Ibid.*, note 28.

105 Edward Hughes/James Snyder, *Litigation and Settlement under the English and American Rules: Theory and Evidence,* (1995) 38 J.L. & ECON. 225, at p. 230.

probability of litigation by raising the costs of unsuccessful claims, is not only in line with economic theory, but also was confirmed by empirical results.[106]

While the loser-pays rule raises the economic stakes and, in theory, thus provides an incentive to incur higher legal expenditures, this rule can and shall be applied in such a way that it improves both time and cost efficiency of arbitral proceedings.[107] Indeed, the cost allocation should reflect the *relative* success and failure of each party, encouraging thereby 'both parties to make their claims as realistic as possible and thus facilitates settlements'.[108] In order to deter, on the one hand, a claimant from adding speculative claims to a strong main claim or inflating a claim, and to discourage, on the other hand, a respondent from adopting dilatory tactics or unreasonable defences, the different issues or sub-proceedings should be 'priced' separately and independently from the ultimate out-come of the case as a whole.[109] It is clear that the desired effect on the parties' conduct – and thus an overall cost saving – can only be achieved if the parties know in advance which principles the arbitrators will follow when allocating costs. The arbitrator should therefore explain the 'rules of the game" at an early stage.

V. DETERMINING THE RECOVERABLE COSTS OF THE PARTIES

If a tribunal comes to the conclusion that costs should be awarded, the amount of costs recoverable by the 'receiving party' from the 'paying party' must first be determined. This is the second limb of awarding costs.

A. The General Principles

While the parties are free to reach an agreement on recoverable costs, arbitration agreements do not normally deal with this issue. Moreover, it is unfortunately not standard practice in international arbitration to discuss cost issues during an organisational meeting at the outset of the proceedings.[110]

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106 *Ibid.*, pp. 235-248.

107 See Michael E. Schneider, *Lean Arbitration: Cost Control and Efficiency Through Progressive Identification of Issues and Separate Pricing of Arbitration Services*, in (1994) 10 Arbitration International 119.

108 John Gotanda, *op. cit.*, p. 26.

109 See Michael E. Schneider, *op. cit.*, p. 135 *et seq.*

110 Apart from the issue of cost deposits, the *UNCITRAL Notes on Organizing Arbitral Proceedings*, UNCITRAL Yearbook, vol. XXVII (1996), do not list costs among the matters to be addressed in an organisational meeting.

Referring to institutional rules will not provide much help either. Instead, the arbitrator must determine which items form part of the recoverable party costs and fix the according amounts on the basis of his wide discretion. There is, however, considerable uncertainty about where the line between allowable and irrecoverable costs should be drawn.

If costs are understood as akin to damages, then a broad view of both the category of allowable items and the recoverable amounts is needed in order to give full compensation to the successful party. At the same time, it is an essential requirement of fairness that if an arbitral tribunal is allowed to require one party to reimburse the other for its litigation expenses that such expenses be limited in some way.

The first precondition for the allowability of party costs may be so obvious that it is rarely spelled out in arbitration rules (or laws): the costs must have been incurred by a party for the specific purpose of the arbitration. Accordingly, a close connection between the cause of the costs and the claim or defence raised before the arbitral tribunal is required. Indirect costs, such as the costs of the disruption of a party's ordinary business due to the arbitration, are thus not recoverable as party costs. Sometimes it is less clear whether a sufficient nexus exists. Different views are taken regarding, for instance, the costs of ancillary court proceedings[111], of legal work done prior to the commencement of the arbitration[112] or regarding costs incurred in connection with settlement negotiations.

Second, the applicable provisions give an indication of what is meant by 'party costs'. In this respect, the wording of the various arbitration rules (and laws) varies and some seem more tolerant than others. For instance, Article 31(1) ICC Rules simply refer to 'the reasonable legal and other costs incurred by the parties', while Article 38 UNCITRAL Rules only mentions 'the costs for legal representation and assistance' and 'the travel and other expenses of witnesses'. The new Swiss Rules have adopted this latter wording. With regard to the UNCITRAL Rules, the more restrictive language has sometimes been understood as an exclusive listing of recoverable costs.[113] At least with

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[111] See, *e.g.*, ICC Case No. 5896 (1992), ICC Ct. Bull., Vol. 4 (1993), p. 38, and ICC Case No. 8445 (1996), (2001) 26 Y.B. Com. Arb. 167-180.

[112] In ICC Case No. 5896 (1992), ICC Ct. Bull., Vol. 4 (1993), p. 38, the tribunal stated that 'the costs of arbitration cannot include costs incurred before the commencement of the arbitration, which by Article 3 of the Rules is for all purposes to be the date when the Request of Arbitration is received by the Secretariat of the Court.'

[113] Rolf Trittmann/Christian Duve, *UNCITRAL Arbitration Rules*, in Practitioner's Handbook on International Arbitration (2002), *ad* Art. 38 UNCITRAL Rules, note 1.

regard to the analogous Article 38 Swiss Rules, and in light of the present practice in Switzerland, it is suggested here that there is no material difference to the 'reasonable legal and other costs' formulation.[114] Neither should recoverable party costs be strictly confined to the two categories expressly listed nor should the words 'costs for legal fees and assistance' be construed as being such fees and expenses as charged by an (external) attorney only. In short, the wording as used in the applicable rules is hardly apt to offer to the arbitrators much guidance.

Finally, only such costs are recoverable which are, from an objective viewpoint, *'reasonable'* or *'necessary'*.[115] The test of reasonableness addresses in essence two questions: were the activities for which the costs were incurred necessary for the arbitration in light of both the complexity of the case and the interests at stake? If so, are the amounts claimed (i.e., the underlying hourly rate and the hours billed) for such activities reasonable? In practice, a certain latitude is inherent in this test. It is not possible for a party to predict with certainty on which points a case will ultimately be decided. Accordingly, the assessment should be made from 'the perspective of the time when the representatives were instructed and not with the benefit of hindsight.'[116] Further, in an international setting, the cost structure of the opposing parties can vary fundamentally, particularly with regard to their costs for legal representation. Hence, the pragmatic fact that a party paid the fees for legal or other professional services not knowing whether it will be reimbursed is 'a strong indication that the amount billed was considered reasonable by a reasonable man spending his own money, or the money of the corporation he serves.'[117]

As a result – and possibly because a scrupulous scrutiny of cost claims may by itself be an expensive exercise – arbitral tribunals regularly adopt a 'broad-brush' approach when applying the test of reasonableness.[118]

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[114] See also Marc Blessing, *Comparison of the Swiss Rules the UNCITRAL Arbitration Rules and others,* Report submitted to the ASA Conference of 23 January 2004, p. 36. There would, for instance, be little justification for not allowing the fees of an accountant whose services were needed for the proper preparation of the case, only because he had not also appeared as an expert witness before the tribunal.

[115] See, *e.g.*, Article 31(1) ICC Rules and Article 28.3 LCIA Rules. ICC Case 8486 (1996), (1999) 24 Y.B. Com. Arb., p. 173.

[116] Michael O'Reilly, *Costs in Arbitration Proceedings* (1997), at p. 64.

[117] Separate opinion of Judge Holtzmann in *Sylvania Technical Sys. Inc.* v. *Government of the Islamic Republic of Iran*, (1985) 8 Iran-U.S. C.T.R. Rep. 329, p. 333.

[118] Alan Redfern/Martin Hunter, *op. cit.*, p. 408.

B. Categories of Parties' Costs

In connection with the preparation and conduct of an arbitration a party may incur, *inter alia*, the following expenditures: the fees and expenses of legal counsel, the fees and expenses of non-legal professional services for the preparation of the case (*e.g.* accountants or property surveyors), the expenses of witnesses and an allowance for their time, the costs of obtaining a private expert opinion, interpreters' and translators' costs, the costs for factual research, general expenses of the party itself (including the costs of travel, accommodation, etc.).[119] In the following, only two aspects are examined in more detail. First, the costs for legal representation because those are usually the most significant item. Second, the party's internal costs: in fact, any services or activities as listed above may be performed, at least partly, by a person employed by the party. It is, however, controversial if in this case such costs remain recoverable.

1. Costs for Legal Representation

The costs of legal representation are recoverable costs provided they are 'reasonable'. Whether the amount claimed is reasonable is a matter to be decided by the arbitrators in the exercise of their discretion and on the basis of objective criteria. The starting point is the amount of fees effectively charged by and paid to counsel. On the one hand, this sum is the upper limit, on the other hand there is 'no good reason *a priori* not to take as a basis the entire alleged costs.'[120] Arbitrators are not bound to apply any local tariffs on attorneys' fees, neither those tariffs in effect at the place of arbitration nor in counsel's homeland.[121] However, when applying the test of reasonableness, arbitrators may take the tariffs and practices in counsel's jurisdiction into consideration. Presumably, those are the basis of the fee-arrangement between the party and its counsel. To the extent that the fees actually paid by the party are in line with such local provisions, this is an indication that they are reasonable.[122]

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[119] See Michael Bühler/Sigvard Jarvin, *op. cit.*, note 41; see also J. Gillis Wetter/Charl Priem, *op. cit.*, p. 253.

[120] Markus Wirth, *op. cit.*, note 60.

[121] See, *e.g.*, ICC Case No. 8786, in 20 ASA Bulletin 1 (2002), at p. 68.

[122] See ICC Case No. 6962 (1992), (1994) 19 Y.B. Com. Arb., p. 193. How should an arbitral tribunal exercise its discretion if a party claims recovery for conditional or contingency fees? Depending on the *lex fori* and the law likely to be applicable to the enforcement of the cost award, arbitrators may have any reason to disregard such fee arrangement. Moreover, the combination of a contingency fee arrangement and the loser-pays rule would mean that, as between the parties to the dispute, the entire cost risk is shifted to one party only. This seems not to be easily reconcilable with a dispute mechanism based on consensus. Michael O'Reilly, *Costs in Arbitration Proceedings* (1997), p. 67 et

In any event, the legal costs claimed should be put in relation to the complexity of the case, the scope and duration of the pleadings, the amount in dispute and the importance of the case for the party.[123] In general, arbitrators can be expected to be slow to substitute their opinion on how much time and effort would have been necessary for the proper preparation and presentation of the case to the decisions taken by a party and its counsel. It is sometimes argued that the fees which eminent attorneys demand should be reduced to the normal fees of a 'hypothetical counsel capable of conducting the particular case.'[124] Again, it is difficult to see what should be the 'right' rate in an international setting since 'party representation costs may vary widely because of a number of reasons, including the vastly different conditions under which lawyers work around the world and the varying ability of lawyers used to their domestic civil procedure to adapt to the often unfamiliar ways of international commercial arbitration.'[125] Further, a high hourly rate does not necessarily result in a high bill, and because a party is free to choose its lawyer, it should not be punished for its choice if successful.[126]

Given these difficulties, the approach regularly adopted by arbitrators is to compare the legal costs of each party.[127] As long as there is no substantial discrepancy between the total sums claimed by each party for legal fees, tribunals tend to intervene only in exceptional cases. Even if the costs of one side are much higher than those of the other, that does not make them unreasonable *per se*. Depending on the case, a party may objectively be forced to incur much higher costs in order to properly present its case.[128]

In those (rather rare) cases, in which the arbitrators came to the conclusion that the legal fees claimed were not justified, the tribunals used different approaches to determine what the 'normal" legal costs would be. In ICC Case No. 5008, the fees of the prevailing claimant's lawyers were four times higher than those paid by the respondent to its attorneys. The tribunal

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seq., suggests that a party who engages legal representatives on a conditional or contingency fee basis may recover a proper amount for costs expended, but that 'clearly this amount should not exceed that payable to representatives working on a time charging basis'.

123 See, *e.g.*, ICC Case No. 11670, published in this issue of the ASA Bulletin, p. 333, cons. 7.9 and seq.; ICC Case No. 6293 (1990), ICC Ct. Bull., Vol. 4 (1993), p. 43.

124 Michael O'Reilly, *op. cit.*, at p. 65.

125 Pierre A. Karrer/Marcus Desax, *Security for Costs in International Arbitration: Why, when, and what if...*, in Law of International Business and Dispute Settlement in the 21st Century (2001), at p. 339.

126 Pierre A. Karrer, *Arbitration saves! Costs: Poker and Hide-and-Seek*, (1986) 3 J. Int'l Arb. 35, at p. 38.

127 See ICC Cases No. 5008 (1992) and 5480 (1991), both in ICC Ct. Bull., Vol. 4 (1993), p. 31/34.

128 For instance, as a consequence of the burden of proof.

thus decided to cut down the recoverable fees to an average between those of both parties' attorneys.[129] In ICC Case No. 5726, the prevailing claimant had instructed three firms of lawyers to act jointly. The tribunal found that it would not be fair if the respondent had to pay for such duplication and therefore assessed the recoverable legal costs on the basis of the claimant instructing two lawyers only.[130]

2. The Party's Own Internal Costs

Executive time: The managers and other staff of a company involved in an arbitration often dedicate substantial time to the case. They will have to spend time on instructing their legal representatives, assisting them with regard to factual issues, attending the hearing, etc. Arbitral tribunals, however, seem reluctant to accept such costs as part of the costs of arbitration. Presumably this perception originates from the somewhat outdated view that before a court, lay parties are 'not allowed anything for their time and trouble, but only for their out-of-pocket expenses.'[131] It is further argued that such executive time is part of the normal costs for running a business enterprise and should therefore not be shifted to the other party.[132] In certain jurisdictions, however, a party may indeed ask to be compensated for its work and loss of time in connection with litigation. Exceptionally, tribunals have thus awarded costs for executive time under reference to such court practice at the place of arbitration.[133] Interestingly, one arbitrator held that, although the time of the claimant's personnel involved in the preparation of the case could not qualify as parties' costs, it may be recoverable as additional damages resulting from the alleged contractual breaches.[134]

In-house counsel in particular: Arbitral decisions show no clear pattern as to the allowability of costs for in-house legal staff. Craig/Park/Paulsson state that:

> 'tribunals are more likely to allow costs disbursed for external consultants and advisers (lawyers, technical experts, economists and

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129 ICC Case No. 5008 (1992), ICC Ct. Bull., Vol. 4 (1993), p. 31.
130 ICC Case No. 5726 (1992), ICC Ct. Bull., Vol. 4 (1993), p. 36.
131 *Jonathan Alexander Ltd* v. *Proctor* [1996] 2 All ER 224, at p. 339.
132 See John Gotanda, *Supplemental Damages in Private International Law* (1998), p. 191. See also ICC Case No. 5029 (1991), ICC Ct. Bull., Vol.4 (1993), p. 32, stating that 'arbitrations inevitably take up time of the parties themselves and their staff, but the cost of any such time is (...) not part of the legal costs of the proceedings'.
133 ICC Cases No. 6345 (1991) and No. 6959 (1992), both in ICC Ct. Bull., Vol. 4 (1993), p. 45/49.
134 ICC Case No. 6293 (1990), ICC Ct. Bull., Vol. 4 (1993), p. 43.

> accountants) than to permit recoupment of a company's internal expenses whether allocated to its legal department or otherwise.'[135]

Several decisions seem to confirm this.[136] Nonetheless, if a party may recover its attorneys' fees from its opponent, why should the costs of an 'in-house' counsel or an internal legal department not be reimbursed? In ICC Case No. 6564, the tribunal held:

> 'There is no justification to privilege a party in terms of costs for the sole reason that it retained outside rather than in-house counsel. (...) A party must be free in allocating the work between outside counsel and its own services. A party which decides to perform most of the preparatory work for the case by its own legal and technical departments should not be placed at a disadvantage compared to one which confers all work to outside counsel and experts.'[137]

This view has now gained increasing acceptance, both in legal writing[138] and in practice.[139] A party's claim for the costs of its in-house legal department may encounter further difficulties:

> 'There is, however, an important difference between the costs of outside counsel and those incurred in-house: the former are expenditures and can be clearly identified and evidenced; in the case of the latter this is not always the case. In view of this difference it appears justified to require some substantiation *inter alia* with respect to the nature of the costs, the personnel involved and type of work performed.'[140]

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135 W. Laurence Craig/William W. Park/Jan Paulsson, *op. cit.*, p. 394.

136 ICC Case No. 5029 (1991), ICC Ct. Bull., Vol. 4 (1993), p. 32; ICC Case No. 6293 (1990), ICC Ct. Bull., Vol.4 (1993), p. 43. In *Andersen Consulting Business Unit Member Firms* v *Arthur Andersen Business Unit Member Firms*, ICC Case No. 9797 (2000), reprinted in 18 ASA Bulletin 3 (2000), p. 514 *et seq.*, the sole arbitrator dismissed a 15 million USD claim for internal employee costs with a single sentence: 'The Tribunal shall not grant [respondents] their internal costs because their allocation of their employees' time and effort to the present arbitration is a decision dependant entirely on the [respondents'] discretion and therefore, these costs must be assumed by [respondents].

137 ICC Case 6564 (1993), ICC Ct. Bull., Vol.4 (1993), p. 46.

138 *E.g.*, Markus Wirth, *op. cit.*, note 60; Michael Bühler/Sigvard Jarvin, *op. cit.*, note 43.

139 See ICC Case No. 8786 (1997), 20 ASA Bulletin 1 (2002), p. 68, in which the tribunal allowed the costs for in-house counsels, apparently as a matter of course. See also Yves Derains/Eric A. Schwartz,*op. cit.*, p. 339 *et seq.*, who state that the allowability of costs for in-house counsel 'appears to be increasingly accepted'.

140 ICC Case 6564 (1993), ICC Ct. Bull., Vol.4 (1993), p. 46.

Accordingly, a party who intends to claim the costs of its in-house lawyers at the end of the arbitration should make sure that the persons involved keep proper time records of the work performed for the arbitration along the lines of what is standard practice for external lawyers. Another question is, how the actual amount of the costs should be computed. The principle that the costs allowed should not exceed the actual and direct costs suggests using the salary of the in-house lawyer, plus arguably a general overhead, as the basis for the computation. On the other hand, one may well assume that 'a party makes no savings by employing in-house lawyers and that the process of determining the recoverable costs should not be further complicated by requiring a successful party to show a detailed breakdown of its internal costs in order to prove what sum will indemnify him in costs.'[141] This would suggest allowing such costs to a successful party 'on the normal basis as if those lawyers were in independent practice.'[142] Again, it may be difficult to find such 'normal basis' in an international dispute. A tentative approach could be to assume that each party's costs for legal work should more or less be in the same range.

What has been said above with regard to in-house counsel would, in principle, also apply to any element of costs in respect of such work done internally which obviated the need for others to do it and hence led to an overall saving of costs. In particular, it will often not only be more convenient, but also cost-effective for a party to have recourse to in-house rather than external technical experts. For various reasons, there may even be no eligible external expert at all. Again, there is no good reason, in principle, to refuse a party the costs of an expert only because this person is an employee.

C. The Procedure

Although the applicable rules will regularly impose an obligation on the arbitral tribunal to decide in what proportion the costs of the arbitration are to be borne by the parties, the arbitrators cannot award party costs if a party neglects to claim such costs.[143] Claims for costs are normally already made in the parties' written submissions, but the final amounts obviously can only be quantified at the very end of the proceedings. Accordingly, the tribunal will normally invite the parties at the end of the final hearings to submit their cost claims, often by way of a simultaneous exchange of submissions. There

[141] Michael O'Reilly, *op. cit.*, at p. 73.
[142] Chartered Institute of Arbitrators, *Guidelines for Arbitrators on Making Orders Relating to Costs of Arbitration*, para. 62.
[143] See Markus Wirth, *op. cit.*, note 59; Michael Bühler/Sigvard Jarvin, *op. cit.*, note 75.

seems to be no standard for such submissions.[144] Some parties just submit a total figure followed by a short breakdown of the different cost items, while others submit copies of all invoices and bills. In this respect, Craig/Park/Paulsson point out that 'recoverable party costs should be considered as similar to an item of damage suffered due to the breaches of contract or tortuous behaviour of the other party, and the amounts claimed should be made subject to proof like any other proof of damage.'[145] Others suggest that the parties should be requested to submit at least a general breakdown of the costs they have incurred, together with a statement of their financial directors confirming that the amount of costs as claimed actually has been incurred and paid.[146] Moreover, it is not unusual for arbitrators to accept outright a lawyer's fee note and only request further evidence for these costs if challenged by the other party.[147]

Several authors submit that each party has a right to be heard with regard to the other party's cost submission; at any rate if a party expressly so requests or if the costs of the party entitled to a cost award are substantially higher than those of the opponent.[148] Indeed, it is general practice to accord each party the opportunity to submit whatever comments they may have regarding the other's cost claim prior to the tribunal's determination of the reasonable party costs.[149]

The decision on costs is normally entered in the last award rendered by the arbitral tribunal because once the final award has been rendered the arbitrator becomes *functus officio*. However, the arbitrator also may include a decision on costs in a partial award resolving certain issues in the arbitration, for instance if the objections to jurisdiction are dismissed. In order to make any decision on costs readily enforceable, it should be made in the format of an award and fix the amount payable by one party to the other in the dispositive of the award by indicating a liquidated sum of money.[150]

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144 Compare ICC Case No. 8032 (1995), (1996) 21 Y.B. Com. Arb., p. 122, ('As for the legal costs incurred by Claimant in the procedure, the Arbitral Tribunal considers that the amount provided by claimant was not supported by any evidence and that, in these circumstances, it was not possible to order defendant to reimburse such fees.') and ICC Case 6564 (1993), ICC Ct. Bull., Vol. 4 (1993), p.46, (where the Arbitral Tribunal found the amount claimed by the Respondent was, in view of the amount of work required, reasonable, although no a breakdown of fees and expenses was provided).

145 W. Laurence Craig/William W. Park/Jan Paulsson, *op. cit.*, p. 394.

146 Michael Bühler/Sigvard Jarvin, *op. cit.*, note 49.

147 See, *e.g.*, ICC Case No. 7006 (1992), ICC Ct. Bull., Vol.4 (1993), p. 49.

148 Stein/Jonas - Schlosser, Sect. 1057 note 13; Markus Wirth, *op. cit.*, note 61.

149 Yves Derains/Eric A. Schwartz, *op. cit.*, p. 341.

150 Michael Bühler/Sigvard Jarvin, *op. cit.*, note 79.

Arbitral awards rarely explain the allocation and determination of costs in great details. Few arbitration laws and rules expressly require a tribunal to state the reasons for their decision on costs. Regarding the situation in Switzerland, the Swiss Federal Court denied that an international arbitral tribunal must provide reasons for its cost decision.[151] Nevertheless, arbitrators should do more to explain their decision on costs and in particular the way they exercised their discretion. Too often the cost issue is disposed of in one or two short sentences and a general reference to the arbitrators' broad discretion. It is ultimately the explanation of the tribunal's motives which gives legitimacy to its decision and helps a party to accept the award. This is not different with regard to cost decisions.

In this context, Article 40.4 Swiss Rules should be noted. It provides that before rendering the award, the arbitral tribunal must submit its draft award to the Chambers 'for consultation on the decision as to the assessment and apportionment of the costs of arbitration'. It can be assumed that this institutional scrutiny will provide an incentive for arbitrators to more adequately explain in the award their decision on costs, and particularly where a tribunal decides not to award the costs in proportion to a party's success. Moreover, it may be hoped that although the Swiss Rules give the arbitrators the widest possible discretion when deciding on costs, this process will be beneficial to distil a 'best practice' approach as to how this discretion should be exercised.

VI. CONCLUSION

Costs are of great importance in international commercial arbitration. However, since most arbitral laws and rules give little guidance to the arbitrators for reaching their decision on costs, the rules and practices as prevailing in national jurisdictions may have a decisive, but unwarranted influence. As a consequence, international arbitration practice has not yet managed to establish a uniform approach to costs and this results in considerable uncertainty for the parties. For this reason, some authors have suggested that the arbitral laws or rules should set precise rules for the treatment of costs which should apply unless otherwise agreed.[152]

As the matters stand, both counsel and arbitrators should address the issue of costs early in order to make the outcome on costs more predictable.

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[151] Decision of 9 June 1998, 4P.99/2000, cons. 5, in 19 ASA Bulletin 1 (2001), p. 102 *et seq.*

[152] See John Gotanda, *op. cit.*, p. 26 *et seq.*; Michael Bühler, *op. cit.*, p. 152.

First, the arbitrators should in good time draw the parties' attention to the tribunal's discretion and, in particular, to the principles it intends to adopt to the allocation of costs if the national law or practice of the parties and their counsel provide for a different approach. This will not only prevent subsequent surprises, but also give the parties the opportunity to reach an agreement on the allocation of costs which corresponds to their own cultural understanding.[153] Second, the issue of recoverability of the costs for work done internally, and in particular regarding the costs of in-house counsel, too, should be clarified as early as possible, for instance at an organisational meeting. Third, the arbitrators will do well to give directions early on regarding the parties' cost submissions and in particular on the required format, but in any event prior to the closing of the hearings. As BLESSING emphasises, the arbitrator should raise these matters with counsel and 'when addressing these issues properly, counsel to both sides will in almost all cases be able to agree on that format'.[154]

Summary:
The decision on costs can have a decisive impact on the overall outcome of a case. However, it is often difficult to predict with any degree of certainty whether and to what extent the successful party will recover its costs at the end of the proceedings. This article gives an overview of the different approaches taken in international arbitral practice regarding cost allocation and looks at the reasons for the lack of a universally recognised principle. It further shows that the arbitrators' wide discretion with regard to both the allocation of costs and the determination of recoverable party costs often means that the decision is prone to be influenced by national practices. Although an analysis of cost awards shows that the outcome of the case is significant for the arbitrators' cost decision, success is not decisive in all cases. The determination of recoverable party costs can add another source of uncertainty. The arbitral precedents leave considerable doubt about whether or not a party may recover its internal costs incurred in connection with the arbitration. Nowadays, arbitrators seem to be more willing to accept at least the costs for in-house counsel as allowable costs if they are sufficiently established. In light of the many uncertainties as to the allocation and determination of costs, these issues should be addressed early in the proceedings in order to avoid subsequent surprises.

[153] Markus Wirth, *op. cit.*, note 58.
[154] Marc Blessing, *op. cit.*, p. 36, fn 35.