

INTERNATIONAL ARBITRATION AND THE ENDS OF APPELLATE REVIEW

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I. INTRODUCTION

The virtual absence of substantive review is one of the most striking features of the arbitration process. Barring unusual circumstances, parties and arbitrators have only one chance to “get it right.” But in international commercial and investment arbitration—fields that tend to involve disputes with significant economic stakes and complex legal and factual issues—the dogma of finality has come under attack, as practitioners and academics have advocated for the introduction of appeals mechanisms.

Proponents of appeals processes in the two arbitration fields do not, however, seek to achieve a wholesale replication of multi-tier adjudication as it exists in national legal systems. In court systems, as many have observed, appellate review fulfills two principal functions: error correction and lawmaking.¹ While these functions are intertwined in operation, the pur-

1. See, e.g., PAUL D. CARRINGTON ET AL., *JUSTICE ON APPEAL* 2 (1976) (identifying “review for correctness” and “institutional review” as the dual functions of appellate review); Christopher R. Drahozal, *Judicial Incentives and the Appeals Process*, 51 *SMU L. REV.* 469, 469–70 (1998) (“The first function of an appeals process is to correct errors by the initial decision-maker. . . . The second function attributed to the appeals process is lawmaking.”); David Frisch, *Contractual Choice of Law and the Prudential Foundations of Appellate Review*, 56 *VAND. L. REV.* 57, 74 (2003) (“[T]he distinction between error correction and law development . . . has been the keystone upon which our whole system of appellate courts has been built.”); Chad M. Oldfather, *Error Correction*, 85 *IND. L.J.* 49, 49 (2010) (“Most depictions of appellate courts suggest that they serve two core functions: the creation and refinement of law and the correction of error.”); Chad M. Oldfather, *Universal De Novo Review*, 77 *GEO. WASH. L. REV.* 308, 316 (2009) (“Appellate courts serve two primary institutional functions—the correction of error in the initial proceedings, and the development of the law.”). Notably, authors consistently call the first function “error correction,” but use a variety of terms for the second function. Terminology is not without significance, and in this case word choice may reflect differing views on the proper place of courts vis-à-vis legislatures. In this Article, unless I address a more specific aspect of the second function, I use the term “lawmaking” in a broad and descriptive sense to refer to the role of courts in shaping substantive law. This includes such diverse activities as the creation of judge-made law, the interpretation

poses they serve are distinct. Error correction protects litigants against erroneous decisions and safeguards the integrity of adjudication. Lawmaking refers to the role of appellate courts in the development and harmonization of norms.

The case for appellate review in each of the two international arbitration fields, on the other hand, targets only one function: error correction in commercial arbitration, and lawmaking in investment arbitration. The primary argument for appeals processes in international commercial arbitration is that parties to high-stakes disputes should have recourse to another adjudicator when awards appear to contain mistakes. In addition, it is expected that the availability of substantive review will attract new parties who currently deem arbitration too risky. The envisioned appeals process typically takes the form of review of awards by a tribunal appointed specifically for this purpose.² In investment arbitration, on the other

of written and unwritten sources of law, the application of law to facts, and the confirmation of the continuing validity of earlier case law.

2. See William H. Knull, III & Noah D. Rubins, *Betting the Farm on International Arbitration: Is It Time to Offer an Appeal Option?*, 11 AM. REV. INT'L ARB. 531 (2000), for an elaborate and compelling argument for offering an avenue for error correction by a second arbitral tribunal within the international commercial arbitration framework. A few years earlier, two international law luminaries had proposed the creation of an international arbitration court, which would hear appeals from commercial arbitration awards. These proposals, however, did not envision substantive review as advocated by Knull and Rubins. *Id.* at 541–42. Rather, they suggested that an arbitration court review awards under the narrow grounds of the New York Convention, see *infra* Part III.A, effectively serving as a substitute for domestic courts in enforcement decisions. See Howard Holtzmann, *A Task for the 21st Century: Creating a New International Court for Resolving Disputes on the Enforceability of Arbitral Awards*, in THE INTERNATIONALISATION OF INTERNATIONAL ARBITRATION: THE LCIA CENTENARY CONFERENCE 109, 112 (Martin Hunter et al. eds., 1995) (proposing a “new court [that] would have exclusive jurisdiction over questions of whether recognition and enforcement of an international arbitration award may be refused for any of the reasons set forth in Article V of the New York Convention”); Stephan M. Schwebel, *The Creation and Operation of an International Court of Arbitral Awards*, in THE INTERNATIONALISATION OF INTERNATIONAL ARBITRATION: THE LCIA CENTENARY CONFERENCE, *supra*, at 115, 115–16 (supporting Holtzmann’s proposed International Court of Arbitral Awards, “whose jurisdiction would be limited to deciding upon challenges to the validity of international commercial arbitral awards.”). See also ELIHU LAUTERPACHT, ASPECTS OF THE ADMINISTRATION OF INTERNATIONAL JUSTICE 112 (1991), for the suggestion that the value of international arbitration “may be enhanced if it is linked to a system of appeal.”

hand, proposals call for the creation of a permanent appeals facility that articulates coherent interpretations of substantive terms in investment treaties. The primary impetus for suggested reforms is a perceived interest of the investment community at large in centralized lawmaking.³

The difference flows, in part, from the distinct nature of the disputes in each field. The paradigmatic commercial arbitration case involves contract claims arising out of business transactions between private parties.⁴ Investment disputes, on the other hand, always involve claims against state party respondents concerning their interference with investments made by foreign investors (often, but not always, in state-sponsored projects).⁵ The private-public distinction also holds true for the sources that govern the disputes. In most commercial

3. See, e.g., Doak Bishop, *The Case for an Appellate Panel and Its Scope of Review*, in 1 INVESTMENT TREATY LAW: CURRENT ISSUES 15, 17 (Federico Ortino et al. eds., 2006) [hereinafter CURRENT ISSUES] (arguing that review by a standing appellate body would contribute to the sustainability of investment treaty arbitration as it would increase consistency and legitimize the process); James Crawford, *Is There a Need for an Appellate System?*, in CURRENT ISSUES, *supra*, at 13, 13 (arguing that an appellate body is needed to address inconsistencies that have arisen as a result of the greatly increased volume of investment arbitrations); David A. Gantz, *An Appellate Mechanism for Review of Arbitral Decisions in Investor-State Disputes: Prospects and Challenges*, 39 VAND. J. TRANSNAT'L L. 39, 74 (2006) ("A well-structured and staffed appellate mechanism could improve the jurisprudence in investment-related arbitration by increasing consistency and annulling the occasional wrong decision."); see also Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521 (2005) (proposing the establishment of an independent, permanent appellate body with the authority to review awards rendered under a variety of investment treaties in order to restore legitimacy, transparency, determinacy, and coherence to investment treaty arbitration).

4. A leading treatise defines "international commercial arbitration" as "a means by which international business disputes can be definitely resolved, pursuant to the parties' agreement, by independent, non-governmental decision-makers, selected by or for the parties, applying neutral judicial procedures that provide the parties an opportunity to be heard," but proceeds to note that "there are almost as many other definitions . . . as there are commentators on the subject." GARY B. BORN, 1 INTERNATIONAL COMMERCIAL ARBITRATION 64–65 (2009) (internal citations omitted).

5. The transactions that may give rise to claims under investment treaties are often referred to as foreign direct investment. One treatise explains: "Foreign direct investment (FDI) typically consists of medium- and long-term infusions of cash, equipment, expertise, or other assets in another country, into either ongoing enterprises or new companies created for the

arbitration cases, arbitrators interpret private contracts. In so doing, they almost always apply the laws of a particular jurisdiction (for example, New York State). Of course, the resulting awards do not contribute to the development of the substantive laws that govern the dispute. In investment arbitration, on the other hand, the sources of both substantive investor rights and the consent to arbitrate are treaties between sovereigns. Investment arbitrators are the primary interpreters of open-ended terms in those treaties. Consequently, their awards contribute to the development of public international law. In light of these characteristics, it makes sense that advocates for appeals processes in commercial arbitration emphasize error correction, which primarily protects litigating parties.⁶ It is also not surprising that lawmaking, which benefits the legal system as a whole, takes center stage in proposals for appellate review in investment arbitration.⁷

This Article addresses an issue that has received surprisingly little attention: Can the proposed appeals processes achieve the error correction and lawmaking goals in the respective arbitration fields? To answer this question, I examine whether the conditions under which each function is realized in court systems are present, or can be replicated, in the relevant arbitration contexts. The examination yields different conclusions for each field. For commercial arbitration, I propose that arbitration institutions offer an optional two-level process that could achieve error correction in a broad sense, aimed at improving the quality of adjudication in the first instance and providing meaningful review for error at the second level. These error correction benefits can only ensue, however, if parties and institutions that opt for appeal are willing to experiment with changes to features that have become common in the arbitration process, including the practice of direct nomination of arbitrators by the parties. As to invest-

purpose of carrying on some business.” CHRISTOPHER F. DUGAN ET AL., *INVESTOR-STATE ARBITRATION 1* (2008).

6. Oldfather, *Universal De Novo Review*, *supra* note 1, at 317 (“[F]ulfillment of [the error correction] function is typically conceived of as involving a focus on ensuring justice between the immediate parties on appeal.”).

7. *Id.* (“The law declaration function . . . involves the articulation and refinement of legal standards through the process of case-by-case adjudication.”).

ment arbitration, I conclude that an attempt to achieve the intended lawmaking goals through the creation of an appeals facility runs into significant problems. In a relatively young field that involves competing interests of a public nature, a certain degree of unsettledness is not only inevitable, but it also provides room for experimentation. Any increased stability that would result from the creation of a permanent appeals facility would come at the expense of the ability to adapt. Moreover, it is doubtful that an appeals facility would achieve the goal of harmonization of investment law. Most investment treaties are bilateral, they currently number approximately three thousand, and their terms are not identical. In addition, unless and until all sovereigns amend their investment treaties to provide for a non-waivable right to appeal, only a sub-set of arbitration awards would be reviewable.

The Article proceeds as follows. Part II examines the different roles of arbitrators in commercial and investment arbitration through the lens of the dispute resolution and public values models of adjudication. Part III analyzes the possibility of error correction in commercial arbitration. Part IV explores whether an appellate mechanism can effectively address incoherence in investment arbitration.

II. TWO ARBITRATION MODELS

This Part provides a brief introduction to international commercial and investment arbitration. Although both fields involve the arbitration of international disputes, they differ in significant respects.⁸ Commercial arbitration is best understood as pure “dispute resolution,” while investment arbitration incorporates elements of a “public values” model of adju-

8. Although the arbitration processes have developed differently due to the distinct nature of the disputes, there is some overlap between the two fields. Some commercial disputes have significant public interest aspects, and the resolution of a commercial dispute may turn on the consequences of mandatory laws or involve evaluation of an executive or administrative decision. See HARRY T. EDWARDS, *Alternative Dispute Resolution: Panacea or Anathema?*, 99 HARV. L. REV. 668, 671 (1986) (“[H]idden in many seemingly private disputes are often difficult issues of public law.”); cf. Gabrielle Kaufmann-Kohler, *In Search of Transparency and Consistency: ICSID Reform Proposal*, 2 TRANSNAT’L DISP. MGMT., no. 5, 2005 at 1 n.2 (pointing out that commercial arbitrations often have a public interest element).

dication.⁹ These differences, in turn, are critical for understanding the envisioned role of appeals processes.

The term “dispute resolution model” refers to the account of adjudication in Lon Fuller’s seminal essay, *The Forms and Limits of Adjudication*, which was written in the late 1950s but officially published posthumously in 1978.¹⁰ The essay identifies as “the distinguishing characteristic of adjudication” that “it confers on the affected party a peculiar form of participation in the decision, that of presenting proofs and reasoned arguments for a decision in his favor.”¹¹ Melvin Eisenberg has termed this claim the “participation thesis.”¹² The dispute resolution component of Fuller’s adjudication model provides a useful framework for understanding the nature of most types of arbitration, including international commercial arbitration.¹³

International commercial cases involve claims arising out of business transactions between two or more parties from different jurisdictions. One leading treatise defines international

9. See Chad M. Oldfather, *Defining Judicial Inactivism: Models of Adjudication and the Duty to Decide*, 94 GEO. L.J. 121 (2005), for an insightful analysis of the debate in the American legal scholarship about the two adjudication models, and how they relate to each other.

10. Lon L. Fuller, *The Forms and Limits of Adjudication*, 92 HARV. L. REV. 353 (1978). Fuller himself did not use the term “dispute resolution model” but it has become a widely used shorthand reference to his account of adjudication. See, e.g., Amanda Frost, *The Limits of Advocacy*, 59 DUKE L.J. 447, 453–54 (2009) (“Lon Fuller is most closely associated with the traditionally adversarial ‘dispute resolution’ model of adjudication, in which private disputes are resolved by a neutral and passive decisionmaker.”); Susan P. Sturm, *A Normative Theory of Public Law Remedies*, 79 GEO. L.J. 1355, 1382 & n.139 (noting that Fuller is generally cited as the “exemplar of the dispute resolution model”).

11. Fuller, *supra* note 10, at 364.

12. Melvin Aron Eisenberg, *Participation, Responsiveness, and the Consultative Process: An Essay for Lon Fuller*, 92 HARV. L. REV. 410, 411 (1978).

13. Indeed, Fuller expressly included arbitration in his definition of adjudication. See Fuller, *supra* note 10, at 354 (noting that “the term adjudication . . . includes adjudicative bodies which owe their powers to the consent of the litigants expressed in an agreement of submission, as in labor relations and in international law”). Fuller was also sensitive to the practices of judges and arbitrators, often using the term “arbiter” when referring to aspects of adjudication that are the same for both but always pointing out differences when relevant. See, e.g., *id.* at 364, 382, 385–93, 397, 401, 407, 409 (references to arbiter); *id.* at 387–88 (explaining why reasoned opinions are not common in certain “arbitration” fields).

commercial arbitration as “a means by which international business disputes can be definitely resolved, pursuant to the parties’ agreement, by independent, non-governmental decision-makers, selected by or for the parties, applying neutral judicial procedures that provide the parties an opportunity to be heard.”¹⁴ Commercial arbitration offers a purer example of the dispute resolution model than almost any court process. This is in large part because arbitrators in international commercial disputes do not contribute to the development of substantive law. In the vast majority of cases, commercial arbitrators apply the laws of specific jurisdictions, often pursuant to a contractual choice of law provision.¹⁵ Thus, an arbitrator called upon to resolve a dispute about a contract governed by

14. BORN, *supra* note 4, at 64–65.

15. For example, the ICC reported that “[i]n the cases filed with the ICC in 2010, the great majority of parties had exercised their freedom to choose the law applicable to the merits by including provisions to that effect in their contracts.” *2010 Annual Statistical Report*, ICC INT’L CT. ARB. BULL., Spring 2011, at 14. The ICC also noted that the parties had opted for national law, as opposed to supra-national law such as the United Nations Convention on Contracts for the International Sale of Goods, in 99 percent of the cases (the report is not clear, however, on whether this is a percentage of all cases filed or of the cases in which the law was specified). *Id.*; see also Christopher R. Drahozal, *Private Ordering and International Commercial Arbitration*, 113 PENN. ST. L. REV. 1031, 1039 n.36 (2009) (presenting a table showing that the percentage of cases in which parties opted for national law was consistently around eighty percent in ICC cases filed between 2003–2007, and concluding that “international arbitration largely is a procedural substitute for national courts; international arbitrators generally apply national law, not some autonomous body of private commercial law.”). In an empirical study, Drahozal found that only 13.6% of the English-language ICC awards published from 1983 through 2002 contained any reference to supranational law, but noted that this number is probably over-inclusive because “[o]nly those awards in which arbitrators have felt least constrained to apply national law have been published.” Christopher R. Drahozal, *Contracting Out of National Law: An Empirical Look at the New Law Merchant*, 80 NOTRE DAME L. REV. 523, 542 (2005) (citing W. LAURENCE CRAIG ET AL., INTERNATIONAL CHAMBER OF COMMERCE ARBITRATION, at 639 n.39 (3d ed. 2000)). Parties almost never authorize arbitrators to act as *amiable compositeurs*, which would empower them to render an award without being bound by strict application of the law. See W. Laurence Craig, *The Arbitrator’s Mission and the Application of Law in International Commercial Arbitration*, 21 AM. REV. INT’L ARB. 243, 267 (2010). The 2010 statistical report of the ICC identifies only one contract in which the parties had so agreed. *2010 Annual Statistical Report*, *supra*, at 14. That commercial arbitrators do not create precedent is also supported by the relative paucity of citation to earlier awards in commercial cases, com-

French law will try to apply this law to the best of his ability, taking account of statutes, decisions from the French courts, expert opinions, and any other relevant materials submitted by the parties.

The contractual underpinnings of commercial arbitration extend to the arbitration process itself. Parties are free to contract for *ad hoc* arbitration or for arbitration administered by an institution. Although institutions offer arbitration rules, the principle of party autonomy allows parties to deviate from most provisions. In this regard, Thomas Stipanowich has observed that “the central and primary value of arbitration is not speed, or economy, or privacy, or neutral expertise, but rather the ability of users to make key process choices to suit their particular needs.”¹⁶ As private adjudicators, commercial arbitrators owe duties principally to the parties who contracted for arbitration, rather than to a broader legal community.¹⁷ The two norms identified by Eisenberg as critical to the dispute resolution function of an adjudicator—attention and “strong responsive[ness] to the parties’ proofs and arguments”—are as apt in the commercial arbitration context today as they were more than thirty years ago.¹⁸

Fuller’s essay has been criticized, perhaps unjustly,¹⁹ for giving insufficient consideration to the public aspects of litiga-

pared to sports and investment arbitration. Gabrielle Kaufmann-Kohler, *Arbitral Precedent: Dream, Necessity, or Excuse?*, 23 *ARB. INT’L* 357, 362–69 (2007).

16. Thomas J. Stipanowich, *Arbitration: The “New Litigation,”* 2010 *U. ILL. L. REV.* 1, 51 (2010).

17. See William W. Park, *Arbitrators and Accuracy*, 1 *J. INT’L DISP. SETTLEMENT* 25, 43 (2010) (contrasting responsibilities of arbitrators and judges).

18. Eisenberg, *supra* note 12, at 411–12. Eisenberg identifies a third norm, namely explanation. He notes, however, that this norm is not critical to dispute settlement or meaningful participation (although it may facilitate these goals), whereas it is a necessary condition for the rulemaking function of adjudication. *Id.*

19. Robert Bone has convincingly argued that the characterization of Fuller’s theory as “dispute resolution” unfairly reduces it to something that has no impact beyond the immediate parties to a dispute. Robert G. Bone, *Lon Fuller’s Theory of Adjudication and the False Dichotomy Between Dispute Resolution and Public Law Models of Litigation*, 75 *B.U. L. REV.* 1273, 1282 (1995) (“Fuller viewed adjudication as a profoundly public institution with a vitally important social function. It was through the process of adjudication that reason was applied to the task of developing frameworks to order the ongoing process of human interaction, including the articulation of public norms.”).

tion. One of the most serious challenges to Fuller's account is Owen Fiss's critique that adjudication's principal purpose is not to resolve disputes, but to articulate public values. The argument is that Fuller's description of the limits of adjudication (the types of disputes appropriate for resolution in the courts) fails to capture the public role of courts.²⁰ For Fiss, the rule-setting aspect distinguishes court adjudication from arbitration: "[T]he *function* of the judge—a statement of social purpose and a definition of role—is not to resolve disputes, but to give the proper meaning to our public values. . . . The function of the arbitrator is to resolve a dispute."²¹

Just as the "dispute resolution" model is useful for understanding the aims of commercial arbitration, Fiss's "public values" model sheds light on how investment arbitration has developed. Investment disputes, which invariably pit investor claimants against state respondents, have a public character. They involve challenges to state action, and a significant portion of investment disputes concern natural resources.²² In investment cases, the basis for the claims and for submission of disputes to arbitration is not a private contract, but rather a treaty between sovereigns. In investment treaties, sovereigns commit to protecting investments made by each other's nationals by granting certain substantive rights (for example, to provide adequate compensation in case of expropriation or to provide "full protection and security" to investments).²³ The commitments are reciprocal, but in the context of a specific investment, the terms "host country" and "investor country"

20. Owen M. Fiss, *Foreword: The Forms of Justice*, 93 HARV. L. REV. 1, 35–37 (1979).

21. *Id.* at 30–31; see also Owen M. Fiss, *Against Settlement*, 93 YALE L. J. 1073, 1086 (1984) (arguing that the job of judges "is not to maximize the ends of private parties, nor simply to secure the peace, but to explicate and give force to the values embodied in authoritative texts such as the Constitution and statutes: to interpret those values and to bring reality into accord with them.").

22. See Karl P. Sauvant, *The Rise of International Investment, Investment Agreements and Investment Disputes*, in APPEALS MECHANISM IN INVESTMENT DISPUTES 3, 13–14 (Karl P. Sauvant ed., 2008) [hereinafter APPEALS MECHANISM] (as of the end of 2006, approximately forty-two percent of investment treaty arbitrations involved the services sector, including infrastructure, with the remaining arbitrations divided equally between manufacturing and natural resources).

23. Franck, *supra* note 3, at 1531–32.

are used to refer to, respectively, the country in which the investment is made and the country of which the investor is a national. Although bilateral investment treaties are patterned on models, their provisions are not identical.²⁴ By interpreting and applying these terms, investment arbitrators contribute to the development of the meaning of these substantive terms.

In contrast with commercial arbitration, investment arbitration has transformed into a hybrid process in which dispute resolution and the articulation of public values go hand in hand. Investment arbitrators are aware of earlier awards and, presumably, mindful of the fact that their own awards will contribute to the development of investment law. Their role in shaping substantive legal norms, unique in the arbitration universe, has been aided by the relative transparency of the field. The International Centre for Settlement of Investment Disputes (ICSID), the only arbitration institution that exclusively administers investment disputes, maintains a website that provides basic information about all pending and concluded cases. Although not all investment awards are published, a significant number are publicly available and easily accessible.²⁵

24. For example, one study of at least five hundred treaties found a variety of approaches to the “fair and equitable treatment” standard, which is absent from some BITs, provided without further qualification in others, but in many BITs is qualified by reference to one of several, potentially not entirely overlapping, standards (by making it subject to “principles of international law,” “international customary law,” the “international minimum standard of the treatment of aliens,” or by combining it with national treatment and most-favored-nation treatment). Anna Joubin-Bret, *The Growing Diversity and Inconsistency in the IIA System*, in *APPEALS MECHANISM*, *supra* note 22, at 137, 137–38. An insightful analysis of the relationship between variation in provisions in investment treaties and seemingly inconsistent results in arbitration awards is provided in Patrick Juillard, *Variation in the Substantive Provisions and Interpretation of International Investment Agreements*, in *APPEALS MECHANISM*, *supra* note 22, at 81. Cf. Barton Legum, *Options to Establish an Appellate Mechanism for Investment Disputes*, in *APPEALS MECHANISM*, *supra* note 22, at 231, 234–35 (noting that even treaty provisions that are facially similar may need to be interpreted differently based on the apparent intent of the negotiating states).

25. Although ICSID does not publish awards without the parties’ permission, it may include excerpts of the legal reasoning of tribunals in its publications. International Centre for Settlement of Investment Disputes Convention, Regulation, and Rules, art. 48, ¶5, Apr. 2006, ICSID 15 [hereinafter ICSID Convention]; International Centre for Settlement of Investment Disputes Rules of Procedure for Arbitration Proceedings, r.48.4, Apr. 2006, IC-

Tribunals increasingly allow submission of amicus briefs by non-parties, and at least one tribunal has opened a hearing to the public.²⁶ Yet commentators have noted an inherent tension between the public nature of the interests at stake in international investment disputes and the private character of arbitration, the forum of choice for resolution of such disputes.²⁷

In investment arbitration, as in national and supra-national court systems, dispute resolution and the articulation of public values are really two aspects of adjudication.²⁸ Although these aspects usually coexist peacefully, they sometimes clash. For example, dispute resolution and the articula-

SID 15 [hereinafter ICSID Arbitration Rules]. In practice, many awards are posted on ICSID's website. See <http://icsid.worldbank.org>; but see Susan D. Franck, *The Nature and Enforcement of Investor Rights Under Investment Treaties: Do Investment Treaties Have a Bright Future*, 12 U.C. DAVIS J. INT'L L. & POL'Y 47, 88–89 (2005) (pointing out that the circumstance that a significant number of investment arbitration awards are not publicly available creates inequality when parties do not have the same access to unpublished awards); see also GUS VAN HARTEN, *INVESTMENT TREATY ARBITRATION AND PUBLIC LAW* 160–64 (2007) (noting the relative transparency of investment arbitration but arguing for compulsory publication of relevant documents and increased openness of process).

26. See, e.g., Andrea K. Bjorklund, *The Emerging Civilization of Investment Arbitration*, 113 PENN ST. L. REV. 1269, 1286–94 (discussing developments toward increased transparency in investment arbitration).

27. See William B. Burke-White & Andreas von Staden, *Private Litigation in a Public Law Sphere: The Standard of Review in Investor-State Arbitrations*, 35 YALE J. INT'L L. 283, 285 (2010) (“[I]t is time to recognize that contemporary investor-state arbitrations are not merely another form of private law commercial arbitration, with one party now being a state, but that they are more fittingly understood as a form of dispute settlement that, like many domestic judicial proceedings, also operates in a public law context.”); see also Nigel Blackaby, *Public Interest and Investment Treaty Arbitration*, in *INTERNATIONAL COMMERCIAL ARBITRATION: IMPORTANT CONTEMPORARY QUESTIONS* 355, 355 (Albert Jan van den Berg ed., 2003); Franck, *supra* note 25, at 69 (“Investment treaty arbitration is . . . a system that grafts a traditionally private dispute resolution system onto an international treaty between Sovereigns.”).

28. Henry Monaghan made this point in discussing the dispute resolution and law declaration aspects of adjudication by the United States Supreme Court. Henry Paul Monaghan, *On Avoiding Avoidance, Agenda Control, and Related Matters*, 112 COLUM. L. REV. 665, 672–73 (2012) (“The Court’s jurisprudence does not formally separate these models. Quite to the contrary, it merges them. . . . But current commentators, although they recognize that the models are only heuristic devices that bleed into one another, tend to emphasize the tensions between the two models.”).

tion of public values may give rise to conflicting demands when the parties misperceive the nature of their dispute, or fail to address relevant legal issues. In such a situation, as Melvin Eisenberg has pointed out, the strong responsiveness norm of the dispute resolution model is at odds with what he calls the “rulemaking function” associated with the public values model.²⁹ An adjudicator could try to reconcile the two models, for instance, by directing the parties to address additional questions. While judges in a constitutional system have strong arguments for bringing up pertinent issues on their own initiative,³⁰ a departure from party control over the scope of a dispute is harder to justify in private adjudication. This is true even for arbitrations that implicate significant public interests.

This tension between the “strong responsiveness” norm and the “rulemaking function” is on display in investment arbitration. True to arbitration principles, investment arbitrators seem at pains to be responsive to the parties’ submissions. Awards typically provide extensive summaries of the arguments made by both sides for each issue, followed by the tribunal’s decision and a discussion of the reasons for coming out in favor of one side over the other. Yet in one of the recent Argentina cases discussed in more detail later in this Article,³¹ an annulment committee criticized a tribunal for its failure to address, *sua sponte*, issues that the parties had not raised. In ruling to annul the award on the basis of manifest excess of powers, the committee stated: “A Tribunal is . . . certainly not required to address arguments that have not been put by parties. . . . Having said that, the Tribunal is required to apply the applicable law, and is required to state sufficient reasons for its decision.”³² In other words, in investment arbitration, it is not

29. Eisenberg, *supra* note 12, at 412–14; *see also* Oldfather, *supra* note 9, at 142 (“Strong responsiveness . . . stands in tension with the lawmaking function.”).

30. *See, e.g.*, Frost, *supra* note 10, at 516–17 (defending issue creation by courts as a condition for the fulfillment of the tasks of courts in giving meaning to disputed legal issues); *see also* Sarah M. Cravens, *Involved Appellate Judging*, 88 MARQ. L. REV. 251, 251–53 (2004) (arguing that appellate judges should be “involved” in guiding a case to the most appropriate outcome, and that they ought to be more transparent in clarifying when they consider theories not presented by the parties).

31. *See infra* Part IV.B.1.

32. *See* Enron Corp. v. Argentine Republic, ICSID Case No. ARB/01/3, Award (May 22, 2007) [hereinafter Enron Award]; Enron Corp. v. Argentine

sufficient to respond to the arguments made by the parties (at least according to the members of this particular annulment committee). Rather, investment arbitrators have an independent obligation to ascertain what the law requires.

The distinction between the dispute resolution and public values models also becomes relevant in determining what the goals of appellate review ought to be. In a pure dispute resolution model, such as commercial arbitration, one would expect a strong focus on the error correction function of appellate review. As we will see, appellate review improves the quality of dispute resolution, not only by correcting errors but also through the disciplining effect of potential reversal on the first instance adjudicators.³³ The lawmaking function of appellate review does not come into play in a pure dispute resolution model, which is concerned primarily with settling particular disputes, not with the external effects of decisions.

In a sophisticated “public values” model, the lawmaking and error correction functions of appeal both serve to articulate communal norms. This is most obviously true for lawmaking, which is simply the manifestation of the articulation of public values at the appellate level. Yet error correction also serves public purposes. In fact, it is somewhat artificial to disentangle the two functions of appellate review, since much of the refinement of law occurs under the guise of error correction.³⁴ Proposals for the introduction of an appeals mechanism in investment arbitration, however, have focused strongly on the lawmaking aspects of appellate review. Advocates for appellate review in investment arbitration are principally concerned with the development of shared understandings. Error correction, at least when applied to legal determinations, is premised on the presumption that the law is relatively settled. In investment arbitration, it is precisely the lack of consensus on fundamental norms that is viewed as problematic. What is argued for is not so much a fresh second look by another panel, but rather the creation of an authoritative entity that establishes the baseline that can then be used to distinguish erroneous decisions from correct ones. For this reason, pro-

Republic, ICSID Case No. ARB/01/3, Annulment Decision (July 30, 2010) [hereinafter Enron Annulment Decision], at ¶¶ 368–78.

33. See *infra* Part III.C.3.

34. Oldfather, *Error Correction*, *supra* note 1, at 64.

posals for appellate review in investment arbitration consistently call for the creation of an appeals facility, as opposed to the appointment of a second tribunal. Error correction, at least at this time, is at most a subsidiary consideration.³⁵

III. INTERNATIONAL COMMERCIAL ARBITRATION AND ERROR CORRECTION

The case for making appellate review more widely available in international commercial arbitration is aimed entirely at the correction of mistakes. Yet the literature has not seriously examined whether it is possible to realize this value in the arbitration context. This Part first provides an overview of the limited substantive review of international commercial arbitration awards that is currently available. It then unpacks how error correction works in court systems and identifies to what extent its central aspects are present, or at least can be replicated, in international commercial arbitration. This analysis culminates in the outline of an optional two-tier process.

A. *The Current Landscape*

It has become a bedrock principle of international commercial arbitration that courts do not second-guess the substantive correctness of arbitral awards. The United States Convention on the Recognition and Enforcement of Foreign Arbitral Awards deserves much of the credit for this state of affairs. Known as the New York Convention, this treaty was signed in 1958 and today has been ratified by 140 nations.³⁶ The New

35. A few authors, however, have discussed the potential role of error correction and accuracy in the argument for the creation of an appeals facility in investment arbitration. See Christian J. Tams, *An Appealing Option? The Debate About an ICSID Appellate Structure*, in 57 BEITRÄGE ZUM TRANSNATIONALEN WIRTSCHAFTSRECHT 5, 26–28 (2006) (discussing “accuracy” as a value served by appellate review, but concluding that this rationale does not justify adding an appellate level because there are no indications that parties question the legitimacy of the current process); Thomas W. Walsh, *Substantive Review of ICSID Awards: Is the Desire for Accuracy Sufficient to Compromise Finality?*, 24 BERKELEY J. INT’L L. 444, 459 (2006) (observing that the desire for accuracy, which directly benefits the parties to the dispute at hand, is a greater incentive for adoption of an appeals procedure than consistency and predictability, which benefit the larger investment community).

36. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Jun. 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter New York Convention]; List of Contracting States, <http://www.newyorkconven->

York Convention distinguishes between the venue of the arbitration, which is typically selected in part for its absence of significant ties to any parties, and the jurisdictions in which enforcement may be sought, in which the losing party has assets. In the latter jurisdictions, the Convention restricts court review by providing an exhaustive list of grounds for refusal of recognition and enforcement of arbitration awards, which does not include error of law or fact.³⁷ The Convention imposes no limitations on review by courts in the venue of the arbitration. However, popular arbitration jurisdictions have severely curtailed their courts' authority to strike down international arbitral awards.³⁸ In addition, several jurisdictions have adopted statutes that recognize waiver of court review of the merits of

tion.org/new-york-convention-countries/contracting-states (last visited Jan. 26, 2012).

37. Most grounds relate to fairness of process or the legitimacy of the arbitration and must be proven by the party challenging enforcement, including invalidity of the arbitration agreement, a party's inability to present his case, excess of the scope of the arbitration agreement, irregularity in the composition of the tribunal, and a decision from a court at the seat of the arbitration setting aside the award. New York Convention art. V, ¶1(a)–(e). The remaining two grounds, non-arbitrability of the dispute and violation of public policy, may be invoked by a party or by the court acting on its own initiative. New York Convention art. V, ¶2(a)–(b).

38. Cf. Thomas E. Carbonneau, *At the Crossroads of Legitimacy and Arbitral Autonomy*, 16 AM. REV. INT'L ARB. 213, 213 (2005) ("The consensus among like-minded national legal systems regarding standards for the court supervision of arbitral awards excludes the judicial review of the merits of awards."). France, for example, limits the grounds for annulment to procedural irregularities or situations in which execution or enforcement would be "contrary to international public policy." Nouveau code de procedure civile [N.C.P.C.] art. 1520 (Fr.). International arbitral awards rendered in Switzerland may be set aside only on procedural grounds or if the award is "incompatible with public policy." BUNDESGESETZ ÜBER DAS INTERNATIONALE PRIVATRECHT, LOI FÉDÉRALE SUR LE DROIT INTERNATIONAL PRIVÉ, LEGGE FEDERALE SUL DIRITTO INTERNAZIONALE PRIVATO [LDIP] [Federal Statute on Private International Law] Dec. 18, 1987, art. 190, ¶2 (Switz.), available in translation at https://www.sccam.org/sa/download/IPRG_english.pdf; cf. Arbitration Act, 1996, c. 23, §§ 69, 81(1) (U.K.) (limiting challenges to arbitral awards based on questions of law to a narrow category of cases and instructing courts to apply a deferential standard of review). In the United States, the Federal Arbitration Act provides an exhaustive list of grounds for vacatur, annulment or modification of awards, and the Supreme Court has ruled that the parties cannot contractually expand these grounds. *Hall Street Assocs. v. Mattel, Inc.*, 552 U.S. 576, 582–91 (2008).

arbitral awards.³⁹ These provisions effectively preclude court review of awards rendered in arbitrations conducted under the auspices of institutions, as arbitration rules typically contain waivers of court review.⁴⁰

The rules of institutions that handle most high-stakes international commercial arbitrations, including the International Chamber of Commerce (ICC) in Paris, the International Centre for Dispute Resolution (ICDR) of the American Arbitration Association (AAA), and the London Court of International Arbitration (LCIA), do not provide for appellate procedures within the arbitration framework.⁴¹ These institutions probably do enforce agreements providing for appellate arbitral review.⁴²

39. *See, e.g.*, N.C.P.C., art. 1522 (parties may waive the right to seek annulment, but such waivers do not affect the right to appeal from a court decision enforcing an award in France); LDIP, art. 192, ¶1 (parties may waive annulment actions or remove some of the grounds for annulment, provided, however, that none of the parties is Swiss); Arbitration Act, 1996, c. 23, § 69(1) (U.K.) (issues of law may be appealed “[u]nless otherwise agreed by the parties”).

40. *See, e.g.*, London Court of International Arbitration, *Arbitration Rules*, art. 26.9, (Jan. 1, 1998) [hereinafter LCIA Rules] (precluding review by courts); International Chamber of Commerce, *Arbitration and ADR Rules*, art. 34, ¶6 (Jan. 1, 2012) [hereinafter ICC Rules] (stating that parties who opt for arbitration under ICC rules “shall be deemed to have waived their right to any form of recourse insofar as such recourse can be validly made” [emphasis added]); *see also* Philip J. McConnaughay, *The Risks and Virtues of Lawlessness: A “Second Look” at International Commercial Arbitration*, 93 Nw. U. L. REV. 453, 467 (1999) (“it has become common for institutions that administer international commercial arbitrations to include provisions in their procedural rules expressly excluding national judicial review of arbitrations they administer”).

41. The rules of these institutions do provide for decision-makers other than the arbitration panel to decide on challenges of arbitrators. ICC Rules art. 14, ¶3 (ICC Court decides on admissibility and merits of a challenge); International Centre for Dispute Resolution, *International Dispute Resolution Procedures*, art. 9 (June 1, 2009) [hereinafter ICDR Rules] (administrator decides on challenge of arbitrator); LCIA Rules art. 10.1–2 (LCIA Court has authority, upon a party’s challenge or a request from the other arbitrators, to revoke appointment).

42. *Cf.* Thomas J. Stipanowich, *Arbitration and Choice: Taking Charge of the “New Litigation,”* 7 DEPAUL BUS. & COM. L.J. 383, 430 (2009) (“Since properly constituted agreements for ‘second-tier’ arbitration are as enforceable as any other arbitration agreements, so are the resulting awards.”). The issue is whether the parties can set aside the finality provisions in institutional rules by providing for a second level of arbitration. Arbitration rules typically pro-

Appellate procedures are currently offered by three arbitration institutions, namely the International Institute for Conflict Prevention and Resolution (CPR), JAMS (formerly an acronym for Judicial Arbitration and Mediation Services, now the official name), and the European Court of Arbitration. These institutions follow the same basic structure, in which a second panel is appointed to review the first panel's award. The rules vary significantly, however, as to the level of deference given to the award of the first panel. The standards of review reflect three philosophies of what appellate review should be, ranging from a check for the most egregious mistakes to a full re-examination of both legal and factual determinations.

CPR is based in New York, but it is involved in the development and promotion of alternative dispute resolution overseas.⁴³ Since 1999, CPR offers a "Rules of Appeals Procedure" which applies if parties have so agreed in writing.⁴⁴ An appellate tribunal consists of three arbitrators, who are appointed by the CPR in accordance with a list procedure.⁴⁵ CPR appears to offer the appellate option reluctantly; its website explains that CPR "does not wish to encourage widespread appeals from arbitration awards."⁴⁶ CPR felt compelled, however, to respond to the concerns of parties to high-stakes

vide that as to the parties, awards are "binding" or "final and binding." ICC Rules art. 34, ¶6; ICDR Rules art. 27, ¶1; LCIA Rules art. 26.9. The AAA, of which the ICDR is a division, offers a model provision that parties who wish to provide for arbitral appellate review can insert in their arbitration agreements. American Arbitration Association, *Drafting Dispute Resolution Clauses: A Practical Guide* 37 (2007), available at <http://www.adr.org/sp.asp?id=29159>.

43. See <http://www.cpradr.org/AcrossBorders.aspx> (last visited May 2, 2012) (portal for information about CPR's activities outside of the United States).

44. International Institute for Conflict Prevention and Resolution, *Rules of Appeal Procedure*, r. 1.1 (2007) [hereinafter CPR Rules of Appeal Procedure]. The appeals procedure seems to target domestic arbitrations, as evidenced by the fact that CPR's roster of appellate arbitrators consists of former federal judges. International Institute for Conflict Prevention and Resolution, *Introduction to CPR Rules of Appeal Procedure*, available at www.cpradr.org. Rule 1.1 provides that the appellate procedure may be invoked only for arbitrations conducted in the United States, but does not expressly restrict it to arbitrations between U.S. parties.

45. CPR Rules of Appeal Procedure, r. 4.

46. International Institute for Conflict Prevention and Resolution, *Introduction to CPR Rules of Appeal Procedure*, *supra* note 44; see also International

arbitrations that a tribunal may render an “aberrant” or “irrational” award, and to make some review available to a losing party that “concludes that it is the victim of a gross injustice.”⁴⁷ To fulfill these limited objectives, CPR’s standard of review is highly deferential: An appellate tribunal may modify or set aside the original award under the limited grounds for vacatur set forth in section 10 of the Federal Arbitration Act,⁴⁸ or if the award “(i) contains material and prejudicial errors of law of such a nature that it does not rest upon any appropriate legal basis, or (ii) is based upon factual findings clearly unsupported by the record.”⁴⁹

JAMS, which was founded in 1979, has long administered arbitrations and mediations through its “Resolution Centers” throughout the United States. JAMS recently established a presence in Europe through the creation of an affiliate called “JAMS International,” which is headquartered in London and also has offices in Amsterdam, Milan, New York, and Rome.⁵⁰ Its Optional Arbitration Appeal Procedure, as the name indicates, applies only upon express agreement. Selection of the appellate arbitrators is left to the parties, but if they fail to reach agreement the assigned case manager is authorized to make the appointments.⁵¹ The appellate panel is mandated to apply “the same standard of review that the first-level appellate court in the jurisdiction would apply to an appeal from the trial court decision.”⁵²

The European Court of Arbitration offers yet another approach. This institution, founded under the patronage of the Council of Europe, disagrees with the “general tendency . . . to

Institute for Conflict Prevention and Resolution, *Commentary on Rules of Appeal Procedure*.

47. *Id.*

48. These grounds include corruption or fraud in the procurement of the award, partiality in the arbitrators, prejudice of the rights of any party as a result of, among other misconduct, a refusal by the arbitrators to hear material evidence, and excess of the tribunal’s powers. 9 U.S.C. § 10(a)(1)–(4) (2006).

49. CPR Rules of Appeal Procedure, r. 8.2.

50. See <http://www.jamsinternational.com/about> (last visited Apr. 23, 2012) (briefly describing JAMS’ mission and history); <http://www.jamsinternational.com/wp-content/uploads/2011/09/JAMS-International-Fact-Sheet.pdf> (last visited Apr. 23, 2012) (listing office locations).

51. JAMS, *Optional Arbitration Appeal Procedure*, art. A (2003).

52. *Id.* art. D.

limit the review of arbitration awards to procedural errors.”⁵³ Appellate tribunals consist of three arbitrators who are appointed by the Court.⁵⁴ Parties are deemed to have agreed to appellate review, unless it is expressly excluded.⁵⁵ The appeals procedure comprises “a full review of the dispute by way of rehearing including dealing in particular with admissibility, the facts and the merits.”⁵⁶

B. *The Case for an Arbitral Appeals Process*

A losing party to a commercial arbitration generally has no avenues for recourse even when it has strong reasons to believe the award is wrong as to an outcome-determinative legal issue. The 2002 Second Circuit decision in *Westerbeke Corp. v. Daihatsu Motor Co., Ltd.* provides an example of such a situation.⁵⁷ The dispute in this case involved a Component Sales Agreement under which Daihatsu, a Toyota subsidiary, was to supply certain engines to Westerbeke, a Delaware corporation that produced engines suitable for use in marine environments.⁵⁸ The contract also granted Westerbeke a right of first refusal as to engines developed by Daihatsu in the future. Westerbeke claimed that Daihatsu had breached that right of first refusal provision when it contracted with a third party for exclusive distribution of a new engine, without offering it to Westerbeke first.⁵⁹ The dispute was submitted to arbitration in New York under the Japan-American Trade Arbitration Agree-

53. The European Court of Arbitration, *Arbitration*, <http://cour-europe-arbitrage.org/content.php?lang=en&delegation=1&id=1> (last visited Mar. 23, 2012).

54. *Arbitration Rules of the European Court of Arbitration*, art. 28, ¶5, available at <http://cour-europe-arbitrage.org/archivos/documentos/22.pdf> (last visited Apr. 15, 2012).

55. *Id.* art. 28, ¶1.

56. *Id.* art. 28, ¶4. The President of the European Court of Arbitration has opined that “the award must be reviewed not only for errors in law but also as to the merits, and that a full review, by rehearing the case, is not just to be tolerated but is to be seen as an important part of the arbitral process.” Mauro Rubino-Sammartano, *Is Arbitration Losing Ground?*, 14 AM. REV. INT’L ARB. 341, 343 (2003).

57. 304 F.3d 200 (2d Cir. 2000).

58. *Id.* at 204 & n.1.

59. *Id.* at 205.

ment, and the proceedings were bifurcated into a liability and a damages phase.⁶⁰

In the interlocutory award on liability, the arbitrator held that Daihatsu had breached the right of first refusal provision because it refused to enter into negotiations with Westerbeke about the new engine.⁶¹ The arbitrator subsequently awarded reliance and expectancy damages, rejecting Daihatsu's argument that New York case law proscribed the award of expectancy damages for breach of a preliminary "agreement to agree."⁶² The arbitrator explained that the right of first refusal provision was more appropriately analyzed as "'a contract with condition precedent to the addition of a new Engine.'"⁶³

A judge in the Southern District of New York vacated the award on the basis of manifest disregard of the law,⁶⁴ ruling that the provision for right of first refusal was a preliminary agreement that could not give rise to expectancy damages under New York law.⁶⁵ The Second Circuit reversed. It reiterated that manifest disregard requires, first, that "the 'governing law alleged to have been ignored by the arbitrators [was] well defined, explicit, and clearly applicable[.]'" and second, that "the arbitrator must 'appreciate[] the existence of a clearly governing legal principle but decide[] to ignore or pay no attention to it.'"⁶⁶ The Second Circuit stated that by determining how to categorize the right of first refusal provi-

60. *Id.*

61. *Id.* at 206.

62. *Id.* at 206–07.

63. *Id.* at 207.

64. Manifest disregard is a judicially created ground for vacatur of arbitration awards that evince the arbitrators' willful defiance of clearly applicable law. Notably, the Supreme Court's opinion in *Hall Street* has cast doubt on the continuing viability of the doctrine. *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758, 1768 n.3 (2010); *see also* Hiro N. Aragaki, *The Mess of Manifest Disregard*, 119 YALE L.J. 1, 3–5 (2009) (providing overview of different positions on the viability of manifest disregard after *Hall Street*). Some have predicted that interest in appeals procedures within the arbitration system will increase as a result of the *Hall Street* decision. *See, e.g.*, George K. Foster & David M. Bigge, *Expanded Review of Awards: A Door Shuts, Others Open?*, N.Y. L. J., Apr. 23, 2008, at 5–6; International Institute for Conflict Prevention & Resolution, *The Calm and the Storm: Arbitration Experts Speak Out on Hall Street Associates*, 26 ALTS. TO THE HIGH COST OF LITIG. 104, 107–08 (2008) (comments by James H. Carter and Robert B. Davidson).

65. 304 F.3d at 208.

66. *Id.* at 209 (citations omitted).

sion, the district court had improperly encroached on the arbitrator's authority to interpret the contract at issue.⁶⁷ The Second Circuit further held that Daihatsu had not demonstrated the existence of a "clearly governing legal principle" precluding categorization of the right of first refusal provision as a contract with condition precedent.⁶⁸ Essentially, Daihatsu had failed to identify a New York case specifically precluding such a reading with regards to a contractual provision that was sufficiently similar to the right of first refusal provision in the Component Supply Agreement.⁶⁹ Yet the Second Circuit strongly suggested that the arbitrator's decision was incorrect. Responding to the argument that, "as a matter of law and sound policy," an agreement to negotiate could never be a contract with condition precedent, the court noted: "[W]ere we confronted with the task of construing the [Components Supply Agreement] in the first instance, we might well be inclined to adopt the reading proposed by the district court, for we have serious reservations about the soundness of the arbitrator's reading of this contract."⁷⁰ The Second Circuit concluded, however, that "our standard of review constrains us to affirm an arbitrator's judgment even if 'a court is convinced he committed serious error.'"⁷¹ Here, the arbitrator's interpretation was "at least slightly colorable, which is all that is required[.]"⁷²

Academics and practitioners who advocate for appellate review in commercial arbitration argue that the losing party in a case like *Westerbeke* should have some opportunity for review, at least when the financial stakes are sufficiently high. They claim that the availability of appellate review within the framework of commercial arbitration would add value for a sizeable percentage of users of arbitration, as well as potential parties who currently do not opt for arbitration because they perceive it as too risky.⁷³ The most articulate defense of this position is

67. *Id.* at 213, 216.

68. *Id.* at 216.

69. *See id.* at 214–15.

70. *Id.*

71. *Id.*

72. *Id.* at 218.

73. While the notion of arbitral appellate review is not universally embraced, many in the arbitration community view it as a more palatable alternative to expanded judicial review. Paul Bennett Marrow, *A Practical Approach to Affording Review of Commercial Arbitration Awards: Using an Appellate*

presented in an article by attorneys William Knull and Noah Rubins, aptly titled *Betting the Farm on International Arbitration: Is It Time to Offer an Appeal Option?*⁷⁴ Stripped down to its essence, their argument is that because of the characteristics of international commercial disputes, parties have a strong interest in an avenue for recourse when they believe an award contains errors.⁷⁵ In the words of a former general counsel:

Arbitrator, 60 DISP. RESOL. J. 10, 12 (2005) (positing that intra-arbitral appellate review is consistent with the underpinnings of arbitration, including flexibility, confidentiality, speed, and efficiency, and eliminates uncertainties relating to judicial review of arbitral awards); Pierre Mayer, *Seeking the Middle Ground of Court Control: A Reply to I.N. Duncan Wallace*, 7 ARB. INT'L 311, 316 (1991) ("It would be perfectly possible to organise a system of *arbitral appeals* which would not present the disadvantages referred to, and which would give the same additional assurance of quality of justice that is sought by creating appellate jurisdictions."); Richard C. Reuben, *Personal Autonomy and Vacatur After Hall Street*, 113 PENN ST. L. REV. 1103, 1140 (2009) (arguing that "[a]rbitral review would not adversely affect the arbitration process to the same degree as public judicial review" because it does not implicate public resources, a second arbitral panel is not confined to the strict standards of review a court would need to follow, and confidentiality can be maintained); Stipanowich, *supra* note 42, at 429–30 ("Appellate arbitration procedures afford parties the opportunity of a 'second look' at an arbitration award in a controlled setting while avoiding the delays and legal uncertainties associated with expanded judicial review."); cf. Chicago Typographical Union v. Chicago Sun-Times, 935 F.2d 1501, 1504–05 (7th Cir. 1991) ("Federal courts do not review the soundness of arbitration awards. . . . If the parties want, they can contract for an appellate arbitration panel to review the arbitrator's award."); but see Eric van Ginkel, *Reframing the Dilemma of Contractually Expanded Judicial Review: Arbitral Appeal vs. Vacatur*, 3 PEPP. DISP. RES. L. J. 157, 201–02 (2003) (arguing that substantive review by courts should not be precluded due to the availability of arbitral appellate review because "[t]he importance of the parties' autonomy simply outweighs the fact that certain scholars (as well as certain contracting parties) may prefer appeal to another arbitral tribunal"). In fact, CPR has expressly justified the introduction of an appeals procedure by stating that it is preferable to substantive court review of arbitration awards. CPR, *Commentary on Rules of Appeal Procedure*, *supra* note 46 (stating that "a well structured private appeal to a highly qualified tribunal is likely to be preferable to seeking judicial review with all the attendant uncertainties.").

74. Knull & Rubins, *supra* note 2.

75. See, e.g., Erin E. Gleason, *International Arbitral Appeals: What Are We So Afraid Of?*, 7 PEPP. DISP. RESOL. L.J. 269, 293 (2007) ("Even arbitrators may be fallible . . . [T]he adoption of appellate procedures for international commercial disputes at an institutional level would enhance the efficiency of international commercial arbitration."); Knull & Rubins, *supra* note 2, at 531–34; cf. Born, *supra* note 4, at 82 (noting as a disadvantage of finality that

“Speed and finality are virtues, but only if you win. They are not virtues if a fundamental mistake has been made.”⁷⁶

Knull and Rubins posit that finality would be an unmitigated advantage only if the stakes were relatively minor, or if arbitrators never made mistakes.⁷⁷ But the prototypical international commercial arbitration involves significant stakes, financially and otherwise.⁷⁸ And of course, arbitrators sometimes make mistakes, just like judges and other humans. In fact, the complexity of the factual and legal issues presented by high-stakes disputes about cross-border transactions may make mistakes *more* likely.⁷⁹ International disputes often present choice of law issues, and may require application of the substantive laws of several jurisdictions.⁸⁰ Also, arbitrators are frequently called upon to apply the laws of a jurisdiction in which they have not trained or practiced.⁸¹ Some features of the ar-

“a wildly eccentric, or simply wrong, arbitration decision cannot readily (if ever) be corrected.”).

76. Thomas J. Klitgaard, Presentation given to the Seventh Annual Transnational Commercial Arbitration Workshop: Transnational Arbitration of High-Tech Disputes (June 20, 1996) *available at* <http://www.wirepaladin.com/spch0696.htm>, *cited in* Knull & Rubins, *supra* note 2, at 563.

77. Knull & Rubins, *supra* note 2, at 541.

78. *Id.* at 537; *see also* David D. Caron, *Reputation and Reality in the ICSID Annulment Process: Understanding the Distinction Between Annulment and Appeal*, 7 ICSID REV. 21, 48–49 (1992) (relating the story of a general counsel who, having been informed of an unfavorable arbitration award with no possibility of appeal, scolded his attorney: “You advised resolving a million dollar dispute with only one roll of the die?”). One commentator noted, in the context of the United States’ refusal to honor party agreements for substantive court review in *Hall Street*: “The tipping point comes, however, when the stakes are so high that parties become unwilling to take the risk that legal principles and rules will not be rigorously applied to their dispute. . . . One way to meet this need is the development of an arbitration appellate panel, the specifics of which would be negotiated by the parties.” International Institute for Conflict Prevention & Resolution, *supra* note 64, at 106–07 (comment by S. Elaine McChesney).

79. Knull & Rubins, *supra* note 2, at 537–38; *see also* Drahozal, *Private Ordering and International Commercial Arbitration*, *supra* note 15, at 1048 (2009) (“In international commercial arbitration, disputes often arise out of non-standardized transactions with very high stakes.”); Van Ginkel, *supra* note 73, at 160 (“[A]s arbitrators are asked to interpret more complex legal issues . . . finality is increasingly felt as the absence of much needed quality control over arbitrators.”).

80. Knull & Rubins, *supra* note 2, at 537–38.

81. *Id.* at 541–42; *cf.* Gleason, *supra* note 75, at 293 (“[A]rbitral awards are sometimes based on misapplications of law . . .”). One commentator

bitration process, including the influence of the parties in the selection process and the fact that most high-stakes disputes are decided by three arbitrators, reduce the likelihood of an aberrational outcome. Yet parties still take a significant risk by leaving the resolution of a dispute in the hands of a single panel.⁸²

Knoll and Rubins argue that one should consider the reasons for choosing arbitration.⁸³ While it may be an exaggeration to say that for transnational disputes, “[a]rbitration is the only game” in town,⁸⁴ the choice for arbitration in this context usually does not emanate from a preference for “alternative” methods of dispute resolution. Rather, the decision tends to be motivated primarily by a desire to avoid problems associated with cross-border litigation, including the perceived “home court advantage,” disputes about jurisdiction, parallel procedures, and difficulties in obtaining enforcement of foreign court judgments.⁸⁵ Thus, in the context of international commercial disputes, traditional arbitration values such as speed, efficiency, and confidentiality arguably take a backseat to the parties’ interest in diligent adjudication.⁸⁶ As a result,

points out that arbitrators trained in different legal cultures may have radically different perspectives on how to interpret the law. James M. Gaitis, *International and Domestic Arbitration Procedure: The Need for a Rule Providing a Limited Opportunity for Arbitral Reconsideration of Reasoned Awards*, 15 AM. REV. INT’L ARB. 9, 19 (2004).

82. Cf. Mauro Rubino Sammartano, *The Fall of a Taboo: Review of the Merits of an Award by an Appellate Arbitration Panel and a Proposal for an International Appellate Court*, 20 J. INT’L ARB. 387, 387 (2003) (“I . . . submit that it may be safer, except for those who prefer to gamble, to provide for a review of the merits in the arbitral agreement.”). One commentator observed that many contracting parties “‘have no confidence that the arbitrators’ decision will be as objective, predictable and correct as one would expect if the decision were made by a highly respected judge sitting without a jury.’” Stephen A. Hochman, *Judicial Review to Correct Arbitral Error: An Option to Consider*, 13 OHIO ST. J. ON DISP. RESOL. 103, 104 (1997), *quoted in* Knoll & Rubins, *supra* note 2, at 541.

83. Knoll & Rubins, *supra* note 2, at 536–37.

84. Jan Paulsson, *International Arbitration is not Arbitration*, 2 STOCKHOLM INT’L ARB. REV. 1, 2 (2008).

85. BORN, *supra* note 4, at 2–3.

86. Caron, *supra* note 78, at 49 (“Because the motivations for entering into international and wholly domestic arbitration can differ, there also perhaps should be important differences in these two forms of arbitration and in how they are evolving. . . . Perhaps internationally, there should be several forms of arbitration, some more courtlike than others, possibly even provid-

international commercial arbitration proceedings often take on features of court litigation. The decision-makers are almost always lawyers rather than industry experts,⁸⁷ the proceedings tend to involve the submission of evidence and legal arguments based on statutes, and awards are reasoned and in writing.⁸⁸

Proponents of appellate review in commercial arbitration usually propose the appointment of a second panel of arbitrators. This is the model selected by the three arbitration institutions that already provide for appellate procedures, although they differ as to the methods for selection of the appellate panel.⁸⁹ Knull and Rubins stress flexibility. They propose that institutions offer templates with different menu options so that parties who wish to opt into appellate review can select the scope and standard of review and procedural restrictions that, for them, strike the right balance between finality and the advantages of a second level of review.⁹⁰

ing for a process of review approaching appeal.”); Nana Japaridze, *Fair Enough? Reconciling the Pursuit of Fairness and Justice with Preserving the Nature of International Commercial Arbitration*, 36 *HOFSTRA L. REV.* 1415, 1416 (2008) (“[I]t is clear that the landscape of international commercial arbitration is changing and the traditional key characteristics of the process, such as speed, cost, informality, and confidentiality, are becoming both less practical and less lucrative.”); see also Knull & Rubins, *supra* note 2, at 538–41. One commentator has gone so far as to conclude that “[t]he notion of efficiency as a value underlying the arbitration of international disputes seems misconceived.” Edward Brunet, *The Core Values of Arbitration*, in *ARBITRATION LAW IN AMERICA: A CRITICAL ASSESSMENT* 3, 21 (Brunet et al., eds. 2006). Knull and Rubins add the observation that finality does not translate into speed, efficiency and cost savings if the losing party puts up protracted fights in the courts to which the victorious party turns for enforcement. Knull & Rubins, *supra* note 2, at 542–43.

87. See, e.g., Stephen R. Bond, *The International Arbitrator: From the Perspective of the ICC International Court of Arbitration*, 12 *NW. J. INT'L L. & BUS.* 1, 5 (1991) (ninety-five percent of arbitrators in ICC arbitrations are legal professionals); Jacques Werner, *The Trade Explosion and Some Likely Effects on International Arbitration*, 14 *J. INT'L ARB.* 5, 10 (1997) (“Arbitral justice in international commercial cases is almost always rendered by business lawyers in private practice, and sometimes by academics.”).

88. BORN, *supra* note 4, at 2; see also Brunet, *supra* note 86, at 21 (“[A]rbitration procedures . . . essentially constitute an event that resembles a trial.”).

89. See *supra* Part III.A.

90. Knull & Rubins, *supra* note 2, at 559–63.

C. *Conditions for Error Correction*

Error correction is the most universal and least controversial purpose of appellate review in court systems. Yet transposing this function into the private dispute resolution context is not a straightforward matter. An examination of the conditions for error correction shows that the implementation of this function into commercial arbitration would require changes to deeply ingrained practices.

1. *The Nature of “Error”*

Error correction, as the name indicates, is premised on the assumption that mistakes can be ascertained. But of course, “error” is a troubling concept. Legal Realists have convincingly argued that, due to the indeterminacy of most legal rules, a range of reasonably “correct” solutions exists for almost any legal question.⁹¹ As put by Karl Llewellyn:

The major defect in [our system of precedent] is a mistaken idea which many lawyers have about it—to wit, the idea that the cases themselves and in themselves, plus the correct rules on how to handle cases, provide one single correct answer to a disputed issue of law. In fact the available correct answers are two, three, or ten. The question is: *Which* of the available correct answers will the court *select*—and *why*? For there is always more than one available correct answer, the court always has to select.⁹²

91. See BRIAN BIX, *JURISPRUDENCE: THEORY AND CONTEXT* 178 (3d ed. 2003) (characterizing Legal Realism as “a critique of legal reasoning: that beneath a veneer of scientific and deductive reasoning, legal rules and concepts were in fact indeterminate and rarely as neutral as they were presented as being.”).

92. Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to Be Construed*, 3 *VAND. L. REV.* 395, 396 (1950); see also Michael Boudin, *Judge Henry Friendly and the Craft of Judging*, 159 *U. PA. L. REV.* 1, 13 (2010) (“[M]any a complicated case is like a jigsaw puzzle with multiple solutions, often as to reasoning and sometimes as to outcome, none being inevitable.”); Jon O. Newman, *A Study of Appellate Reversals*, 58 *BROOK. L. REV.* 629, 630 (1992) (“Reasonable judges will inevitably come out differently on close questions of law. The hierarchical structure of a judicial system requires that even a well-reasoned view of a trial judge will be displaced by the well-reasoned view of a panel of appellate judges.”).

Some Legal Realists have argued that the indeterminacy of law enables adjudicators to characterize rules and past decisions so as to fit the result they want to reach.⁹³ From the existence of a range of possible outcomes, it does not necessarily follow that a judge's personal preferences will determine the outcome. It does mean, however, that error is often a debatable matter. Moreover, as a matter of logic, one might expect that a relatively large number of appeals are taken from decisions about which reasonable legal minds could disagree.⁹⁴ Inevitably, at times the determination of error on appeal appears arbitrary.⁹⁵

The Realist notion of indeterminacy rings particularly true for determinations that involve discretion and, as a result, a certain level of subjectivity. Examples are factual determinations that turn on credibility judgments, or interpretation of ambiguous contractual language. These are, of course, precisely the types of determinations commercial arbitrators must make. The international context may compound the difficulties. Consider the assessment of the intent of two or more parties at the time they entered into the contract. This is already a challenging task in the case of parties who negotiated against

93. See generally JEROME FRANK, *LAW AND THE MODERN MIND* (1930) (discussing rationalization in judging and the potential influence of a judge's personality and biases); KARL N. LLEWELLYN, *THE BRAMBLE BUSH: ON OUR LAW AND ITS STUDY* 67-70 (1930) (describing how courts use precedent to de-emphasize unfavorable cases and bolster favorable ones).

94. The theory is that relatively few appeals are taken from decisions that are clearly correct, leaving decisions that are clearly incorrect and decisions whose accuracy is debatable. But see Harlon Leigh Dalton, *Taking the Right to Appeal (More or Less) Seriously*, 95 *YALE L.J.* 62, 85 (1985) (identifying several factors that facilitate appeal, including access to counsel, a strong interest in the outcome, strategic considerations, and a belief that the first instance decision was erroneous, and noting that with the exception of the last one, none of them relates to the merits of the dispute).

95. In a study of reversals by the Second Circuit, Judge Newman concluded that "the overwhelming proportion of the reversals arose from disagreements between the Second Circuit and a district court on a reasonably debatable point of law. Arguably, the number of reversals of that sort indicates that the law is less determinate than one would wish, but it does not indicate to me that either the district courts or the Second Circuit are performing deficiently." Newman, *supra* note 92, at 638. Cf. Steven Shavell, *The Appeals Process as a Means of Error Correction*, 24 *J. LEGAL STUD.* 379, 413 (1995) (noting that errors involving the application of law to facts "are conceptually clear when the law is well-articulated, but often the law will not be specified in a relevant aspect and must be amplified.").

the backdrop of shared legal norms. When parties hail from different legal cultures, however, there is a stronger likelihood that they have incompatible notions of what was agreed, even if they engaged in extensive negotiations and all parties believe they fully understood the documents they were signing.⁹⁶ Such parties may also have different ideas about how contractual gaps are to be filled in, which is critical in long-term contracts that cannot provide for all contingencies.⁹⁷ In many civil law traditions, for example, a good faith principle is used in connection with the interpretation of contractual terms as well as to supplement the agreement (playing a role similar to, but not identical with, the “implication of terms” doctrine in common law). In some legal systems, good faith may even operate to set aside express contractual terms in exceptional circumstances—a result that could be baffling to many business people and lawyers from common law jurisdictions.⁹⁸

Moreover, arbitration, even when it involves international disputes, differs from litigation, and arbitrators are not judges. Consequently, as pointed out by Laurence Craig, “the result in many cases will be the application of an approximation of the national law rather than the application of the national law precisely the same way a court of that jurisdiction would apply it.”⁹⁹ In part, this is because unlike judges who are steeped in a particular legal culture, commercial arbitrators often apply the laws of a jurisdiction with which they are not intimately familiar. It is to be expected that the arbitrators’ training in and experience with other legal systems colors their interpretation of the contracts and the applicable law.¹⁰⁰

The notion that arbitrators are law applicers, not lawmakers, presents a challenge to the argument for appellate

96. Cf. Lawrence Solan et al., *False Consensus Bias in Contract Interpretation*, 108 COLUM. L. REV. 1268, 1269 (2008) (“[T]he parties to a contract may understand their rights and obligations differently and never notice the differences until a disagreement occurs . . .”).

97. Cf. Katharina Pistor & Chenggang Xu, *Incomplete Law*, 35 N.Y.U. J. INT’L L. & POL. 931, 957–59 (2003) (discussing incomplete contract theory).

98. See Arthur Hartkamp, *The Concept of Good Faith in the UNIDROIT Principles for International Commercial Contracts*, 3 TUL. J. INT’L & COMP. L. 65, 65–66 (1995) (noting that application of the doctrine good faith may lead to the setting aside of an entire contract or the non-application of otherwise applicable, even perhaps mandatory, statutory rules).

99. Craig, *supra* note 15, at 256.

100. Cf. *id.* at 255–56.

review in international commercial arbitration. This is especially true when the applicable law does not specifically address an issue. When presented with a lacuna in the governing law, an appellate court does not need to accord any deference to the solution adopted by the trial court. It can simply identify a different principle or rule and declare that the lower court's decision was erroneous. The justifications for such intrusive review, however, are less strong when the lawmaking function of appellate review falls away. The *Westerbeke* decision, discussed above, touches on this issue in the context of a discussion of the constraints imposed on court review of arbitral awards. Daihatsu had asked the Second Circuit to hold that as a matter of law and principle, a provision that was interpreted to impose a duty to negotiate could not simultaneously be a contract with condition precedent.¹⁰¹ The Second Circuit observed:

[O]ur announcement of such a principle, no matter how well-founded, would not affect the outcome of this case. Our sole task is to determine whether there *already* exists a well-defined, clearly governing decisional rule under New York law that would prohibit the arbitrator from reading the [Components Supply Agreement] as a contract with condition precedent. Daihatsu has not met its burden of showing that such a rule exists.¹⁰²

Of course, the existence of a lawmaking function bolsters the case for plenary review, especially on questions of law. Conversely, the absence of this function in arbitration arguably would call for a more limited concept of error, according greater deference to the first tribunal.¹⁰³ When no unequivocal rule can be identified, why substitute the second tribunal's speculation on which decision is most in keeping with the law for that of the first tribunal? This discomfort is probably one of the reasons why advocates for appellate review have proposed deferential standards of review. Arguably, *de novo* review

101. 304 F.3d at 215–16.

102. *Id.* at 216.

103. *Cf.* Oldfather, *Universal De Novo Review*, *supra* note 1, at 318–19 (pointing out that review under a more deferential standard is still review for error, but “[t]he difference would lie in the manner in which error is defined.”).

(especially in the United States, where it only pertains to legal issues) is primarily necessary to ensure harmonized application of the law within a jurisdiction. When appellate review does not serve that function, it is not self-evident that an appellate tribunal should have the authority to “correct” a decision from the lower tribunal with which it disagrees but that is not blatantly wrong.

On the other hand, even when there is no rule that is technically on point, courts and arbitrators still have an array of tools to determine which solutions are most in line with the applicable law. Among other things, they may draw on general legal principles, rules governing analogous situations, implicit assumptions in the existing case law, and rules adopted in other jurisdictions. And although disputes that raise questions of first impression are in some ways distinct from those in which there may be reasonable disagreement about how the law applies to a given situation, both types of cases require adjudicators to try to determine which result is most accurate in light of the surrounding legal context. If one accepts that adjudicators are capable of qualitatively assessing different defensible answers, the error correction function standing alone provides a strong justification for a more searching standard of review on appeal.

2. *Error Correction and Hierarchy*

Proponents of the introduction of appeals processes into international commercial arbitration, as noted, appear to struggle with the question of why the decision of a second panel would have more authority than the award rendered by the first panel. One of the main issues in developing a meaningful review mechanism within commercial arbitration, therefore, is whether error correction can be disentangled from hierarchy.

In jurisdictions with a multi-level court structure (which describes the legal system of virtually all nations),¹⁰⁴ appellate review is embedded in, and identified with, institutional hier-

104. See Peter E. Herzog & Delmar Karlen, *Attacks on Judicial Decisions*, Ch. 8 in CIVIL PROCEDURE 69, in INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW (Mauro Cappelletti ed., 1982); Shavell, *supra* note 95, at 379; but see MARTIN SHAPIRO, COURTS: A COMPARATIVE AND POLITICAL ANALYSIS 194–222 (1981) (describing limitations on the use of appeals under Islamic law).

archy.¹⁰⁵ Indeed, the hierarchical structure itself confers some degree of authority on the decisions of appellate courts. But court systems have also put structural features and procedural practices in place that provide credibility to the notion that decisions by intermediate appellate courts are “better” than the ones they purport to correct. One such feature is the increase in the number of adjudicators: in many systems, a dispute will first be heard by a single adjudicator and can then be appealed to a three-member panel. In commercial arbitration, on the other hand, it is common to submit high-stakes disputes immediately to a panel of three arbitrators.¹⁰⁶

The hierarchy in court systems effectively creates a division of labor between the different actors. In the federal court system of the United States, in theory, the primary function of intermediate appellate courts is to correct errors made by the trial courts, while the Supreme Court has the ultimate responsibility for harmonizing the interpretation and application of federal law.¹⁰⁷ The reality, of course, is more complex. Because the Supreme Court takes on a fraction of the cases that present unsettled questions of law, in practice intermediate appellate courts play an important role in the development of legal standards.¹⁰⁸ As a result, there is variation among the Circuits in the interpretation of federal law.

The rules governing appellate review reflect the need to balance competing values, including accuracy and efficiency. One of the most important choices to be made in designing an

105. Lea Brilmayer, *Wobble, or the Death of Error*, 59 S. CAL. L. REV. 363, 381 (1986) (“Error amounts to an inconsistency between the decision made and the applicable standards. One cannot have error without hierarchy . . . Characterizing a legal decision as error is possible within an established hierarchy because in such a hierarchy there is an accepted direction of fit; the lower court’s judgment is supposed to fit the appellate court’s.”).

106. See, e.g., MARGARET L. MOSES, *THE PRINCIPLES AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION* 117 (2008) (noting that “[i]n international arbitrations, there is frequently a preference for three arbitrators” for high-stakes disputes).

107. See Frisch, *supra* note 1, at 74–75 (arguing that the trial court is assumed to be primarily responsible for correcting errors in the trial court, so that the supreme court can concentrate on developing a useful body of law).

108. See Benjamin Kaplan, *Do Intermediate Appellate Courts Have a Lawmaking Function?*, 70 MASS. L. REV. 10 (2007) (arguing that, although the extent varies depending on the extent to which the highest court exerts control, intermediate courts contribute significantly to the development of law).

appeals process is how to divide the responsibilities between the first instance adjudicator and the appellate adjudicator. Court systems have adopted different approaches. For example, one significant difference between appellate review in the United States and in continental European legal systems concerns the treatment of facts. In the United States, appellate courts review legal questions *de novo* (i.e., they engage in plenary review of these questions), and factual determinations made by a trial court judge under a highly deferential “clearly erroneous” standard.¹⁰⁹ Historically, the justification for the existence of two standards of review “rests upon the belief that different tiers of courts possess different decision-making skills and that this distinction recognizes the particular competence of each.”¹¹⁰ The pre-trial and trial stages are characterized by a strong emphasis on the development of a factual record. The adversary system empowers parties to leave no stone unturned in the discovery process, and even before trial, parties have the opportunity to present evidence in connection with summary judgment motions, and sometimes at preliminary injunction hearings. Trials often involve extensive questioning of fact and expert witnesses by counsel for all parties, and in high-stakes commercial cases, they can easily take several days or even weeks. The near-exclusive focus on legal issues at the appellate level suggests that the legal system of the United States primarily values appellate review for its role in lawmaking. Because determinations of fact rarely have significance for anyone other than the parties to a specific dispute, it makes sense to devote fewer appellate resources to this review for factual errors.¹¹¹ Civil law systems, in contrast, do not have distinct standards of review for factual and legal issues, at least not formally. In continental European court systems, appellate courts may request evidence and hear witnesses, and they

109. FED. R. CIV. P. 52(a)(6). Factual findings from juries are generally insulated from review under the Seventh Amendment. U.S. Const. amend. VII.

110. Frisch, *supra* note 1, at 77.

111. See LLEWELLYN, *supra* note 93, at 36 (noting that if imposing consistency is the main function of appellate review, “then a review of the facts, of the doubtful testimony, even a review of all the details of admitted facts, in reference to the legal consequences, seem to lose their importance. What looms large is the *rule* to be laid down—a general proposition.”); cf. Frisch, *supra* note 1, at 78–79.

are not bound by the trial court's factual findings.¹¹² Thus, in legal traditions that do not have a formal precedent system and in which the legislature has primacy in developing new law, appellate courts engage in a more comprehensive form of error correction.¹¹³ The absence of lawmaking in international commercial arbitration would similarly remove some of the justifications for treating factual findings and legal conclusions differently.

A more mundane aspect of hierarchy is that judges operate in a system in which the higher levels come with increased prestige. Of course, at an individual level, certain trial court judges may be held in higher esteem than most or even all appellate court judges in a given jurisdiction. Nonetheless, in many legal systems the advancement of a trial court judge to the appellate level is viewed as a promotion.¹¹⁴ In arbitration, in contrast, it is hard to conceive of a class of appellate arbitrators. To be sure, the international arbitration community has as many ranking lists of arbitrators, firms, and attorneys as any other field.¹¹⁵ Yet unless and until appellate review becomes

112. See, e.g., MARY ANN GLENDON ET AL., *COMPARATIVE LEGAL TRADITIONS* 190 (2d ed. 1994) (noting that in civil law court systems, "the proceedings in this intermediate court may involve a full review *de novo* of the facts as well as the law of the case."); CIVIL APPELLATE PROCEDURES WORLDWIDE 161–62 (Charles Platto ed., 1992) (in France, an appeal transfers the entire matter to the appellate court, with respect to both questions of fact and law, essentially resulting in a "*de novo* trial" as to the aspects from which appeal is taken); *id.* at 179–80, 206–07 (describing similar basic outlines in Germany and Spain).

113. Mirjan Damaska has famously characterized civil law system as primarily "hierarchical," versus the more "coordinate" nature of common law systems. See MIRJAN R. DAMASKA, *THE FACES OF JUSTICE AND STATE AUTHORITY* 18–28 (1986). He notes that in a hierarchical structure, "[t]here are few aspects of lower authority's decision making that are accorded immunity from supervision: fact, law, and logical are all fair game for scrutiny and possible correction." *Id.* at 48–49.

114. Indeed, one of the central presumptions in empirical research on incentives of judges is that they are assumed to be motivated by a desire for promotion, understood as advancement to the next level in the court hierarchy. See, e.g., Drahozal, *supra* note 1, at 476–77; Richard A. Posner, *What Do Judges and Justices Maximize? (The Same Thing Everybody Else Does)*, 3 *SUP. CT. ECON. REV.* 1, 6 & n.9 (providing an overview of studies that analyze the behavior of judges in utility-maximizing terms, including the desire for promotion).

115. See, e.g., CHAMBERS & PARTNERS, <http://www.chambersandpartners.com> (last visited Mar. 22, 2012) (providing rankings of international arbitra-

commonplace in commercial arbitration, arbitrators have no financial incentives to serve only on appellate panels. The practice in which each side nominates an arbitrator and the two party-appointed arbitrators select a chair adds further complications. Why should a second tribunal have the power to correct “mistakes” made by what the parties considered to be the best available tribunal at the time of appointment?¹¹⁶ To put it bluntly, within the current arbitration framework, the best guarantee against a rogue tribunal is not to appoint one.

The absence of a formal hierarchy thus poses challenges to the implementation of appellate review in commercial arbitration. For an appeals system to work in this context, parties and institutions will have to be willing to create conditions that will lend added legitimacy to rulings made at the second level.

3. *Quality of Adjudication*

One aspect of error correction is the notion that appellate review improves the quality of adjudication. It does so in two ways. First, appellate courts are generally better equipped than trial courts to reach well-thought-out decisions on questions of law. Second, the awareness that another court may review a decision creates incentives for more diligent decision-making at the lower level. Appellate review thus facilitates error correction as well as error avoidance.

Court systems are structured so as to ensure that appellate courts can engage in more careful deliberation on legal issues than trial courts. Take, for example, the increase of the number of judges on appeal discussed above. There is a persistent

tion practices at law firms); Global Arbitration Review’s “GAR 100,” <http://www.globalarbitrationreview.com/surveys/survey/156/GAR-100> (last visited Mar. 22, 2012); Global Arbitration Review, *The International Who’s Who of Commercial Arbitration*, <http://www.whoswholegal.com> (last visited Mar. 22, 2012); *Euromoney’s Guide to the World’s Leading Experts in Commercial Arbitration*, <http://www.expertguides.com> (last visited Mar. 22, 2012). This type of recognition is proudly relayed in practice group descriptions and bios of individual practitioners.

116. See Mark D. Wasco, *When Less Is More: The International Split Over Expanded Judicial Review in Arbitration*, 62 RUTGERS L. REV. 599, 620–21 (2010) (“There is no guarantee that the addition of an appeal process will give any more protection against ‘maverick’ decisions.”); cf. Shavell, *supra* note 95, at 391 (suggesting that the existence of the appeals process may spur judges to expend effort toward greater accuracy at trial).

belief that three judges are more likely to reach a correct outcome than one. Indeed, one empirical study, which compared reversal rates by the federal courts of appeal of appellate bankruptcy law decisions made by sole judges (district courts judges) and by three-judge panels (three-member panels of bankruptcy judges), supports the notion that a perception exists among judicial actors that multi-member appellate panels are more likely to arrive at the right outcome.¹¹⁷ The theoretical literature puts forward two reasons for this intuition. First, as a matter of statistical probability, a three-judge panel reduces the risk of a truly erratic decision as it would require two judges to sign onto it.¹¹⁸ The second reason is the idea that collective deliberation improves the quality of decision-making.¹¹⁹ Paradoxically, the two arguments rest on conflicting premises. The first reason for why three adjudicators are better than one assumes that each decision-maker decides independently. The second reason, on the other hand, acknowledges the reality that decision-making on a multi-member

117. Jonathan Remy Nash & Rafael I. Pardo, *An Empirical Investigation into Appellate Structure and the Perceived Quality of Appellate Review*, 61 VAND. L. REV. 1745, 1803–06 (2008).

118. This argument is a variation of the Condorcet Jury Theorem, which explains that “where each voter has more than an even chance of being right on some matter, then the more voters we have, the closer we get to a probability of one getting the matter right by abiding by a simple majority vote.” Saul Levmore, *Ruling Majorities and Reasoning Pluralities*, 3 THEORETICAL INQUIRIES IN LAW 87, 88–89 (2002); cf. Evan Caminker, *Why Must Inferior Courts Obey Superior Court Precedents?*, 46 STAN. L. REV. 817, 847 (1994) (“Assuming (quite reasonably) that each individual judge has a greater than fifty percent chance of arriving at the ‘correct’ answer in any given legal dispute, then the larger the panel the greater the likelihood that a majority of them will reach the correct result . . .”); Paul D. Carrington, *Crowded Dockets and the Courts of Appeals: The Threat to the Function of Review and the National Law*, 82 HARV. L. REV. 542, 551 (1969) (“By employing a larger group of decision makers than can be efficiently employed at the primary level, we bring a broader base of values into operation so that the personal dimension of decisions is diminished.”).

119. See, e.g., Lewis A. Kornhauser & Lawrence G. Sager, *Unpacking the Court*, 96 YALE L. J. 82, 102 (1986) (describing some effects of the exchange of ideas and concluding that “the general assumption favoring deliberation as an aid to correct judgment seems reasonable in light of common experience.”); Alex Kozinsky, *What I Ate for Breakfast and Other Mysteries of Judicial Decision Making*, 26 LOY. L.A. L. REV. 993, 994 (noting the constraining influence provided by the need for a federal appellate judge to “persuade at least one colleague, preferably two, to join your opinion.”).

panel does not come down to a simple aggregation of the individual adjudicators' votes. The collegial nature of the undertaking inevitably affects—some would say distorts—the decision-making process of each individual adjudicator.¹²⁰ Even if there were no true collective deliberation, an adjudicator's perceptions regarding the other members' positions may influence her vote. The exchange of views between multiple decision-makers further increases the likelihood that the result ends up being different from what the aggregation of three independent decisions would have yielded.¹²¹ So, the collegial nature of multi-member courts presents the risk that a decision-maker who favors an aberrational result convinces at least one other member of a panel to change his or her mind (perhaps because the first person is more authoritative, or simply happens to speak when others have not fully made up their minds).¹²² In sum, although the exchange of insights about a case may improve decision-making, it offsets to some extent the notion that three minds are better than one.

The nature of appellate decision-making also facilitates a strong focus on legal issues.¹²³ By design, appellate judges are

120. See, e.g., Lewis A. Kornhauser & Lawrence G. Sager, *The One and the Many: Adjudication in Collegial Courts*, 81 CALIF. L. REV. 51–56 (1993) (discussing reasons for strategic voting on multi-member courts); Evan H. Caminker, *Sincere and Strategic Voting Norms on Multimember Courts*, 97 MICH. L. REV. 2297, 2312–33 (detailing opportunities and incentives for strategic conduct).

121. Kornhauser & Sager, *supra* note 119, at 100–02; Tracey E. George, *Developing a Positive Theory of Decision-making on U.S. Courts of Appeals*, 58 OHIO ST. L. J. 1635, 1655–65 (1998) (discussing “strategic” theories of judicial behavior, which analyze the influence of several factors, such as interactions with colleagues on the court, on decision-making).

122. Cf. Levmore, *supra* note 118, at 90 (noting that “[a Condorcet] Jury Theorem purist might say that the simple result is ruined if voters are given the opportunity to influence one another . . . , to exhibit herd mentality, or to otherwise allow their own assessments and self-esteem to interfere with the value of numerosity.”); Menachem Mautner, *Luck in the Courts*, 9 THEORETICAL INQUIRIES IN LAW 217, 228 (2008) (“Allowing the judges in the panel to be influenced by their colleagues undermines the rationale for having judicial decisions made by a large panel.”); Maxwell L. Stearns, *The Condorcet Jury Theorem and Judicial Decision-making: A Reply to Saul Levmore*, 3 THEORETICAL INQUIRIES IN LAW 125, 147 (2002) (expressing skepticism about the significance of the Condorcet Jury Theorem for understanding appellate court decision-making).

123. Caminker argues that even if higher courts have stronger proficiency for many of the reasons I mention, the comparative disadvantage of lower

free from many of the interruptions trial court judges face, such as short-notice applications for emergency relief, case management, and in the United States, discovery disputes. A trial court judge lives with a case until it is finally disposed of or the parties settle the matter. Appellate judges, in contrast, have one-off encounters with cases. After reviewing the lower court record and the parties' submissions on appeal and possibly hearing oral argument, they write an opinion, and that typically concludes their involvement. In addition, the two standards of review, at least in theory, make it possible for appellate judges in the United States to concentrate on legal issues without bearing responsibility for making independent factual determinations.¹²⁴ Even in civil law systems, which have not formalized the division of labor to the same extent, appellate courts often engage in less extensive fact-finding than the trial courts.¹²⁵ And of course, appellate judges enjoy the benefit of an opinion from a lower court judge who has grappled with the pertinent legal issues. Relatedly, one would expect that the party submissions on appeal are at once more focused, in the sense that they address the most problematic parts of the lower court's opinion, and better developed.¹²⁶

courts is less pronounced once a higher court has addressed a legal issue. Caminker, *supra* note 118, at 848–49. But in many cases, even if a higher court has decided a legal question, the precise scope of the decision as well as its application to specific cases could still be unclear.

124. See *Salve Regina Coll. v. Russell*, 499 U.S. 225, 231–32 (1991) (“District judges preside alone over fast-paced trials: of necessity they devote much of their energy and resources to hearing witnesses and reviewing evidence . . . Courts of appeals, on the other hand, are structurally suited to the collaborative judicial process that promotes decisional accuracy. With the record having been constructed below and settled for purposes of the appeal, appellate judges are able to devote their primary attention to legal issues.”); see also Frisch, *supra* note 1, at 77–78 (citing *Salve Regina* and noting the “widespread and persistent belief that appellate judges are more likely to generate the correct answers to questions of law than their brethren below who oversee the trial and provide the initial answer to all legal questions, both simple and difficult.”).

125. See GLENDON ET AL., *supra* note 112, at 190 (intermediate appellate court panels in civil law systems initially determine the facts based on the trial court record, but they may question witnesses again or request the parties to submit new evidence).

126. Cf. *Salve Regina*, 499 U.S. at 232 (“As questions of law become the focus of appellate review, it can be expected that the parties’ briefs will be refined to bring to bear on the legal issues more information and more comprehensive analysis than was provided for the district judge.”).

Appellate review also improves the quality of adjudication in a more indirect way, through its restraining influence on first instance judges.¹²⁷ The threat of reversal provides powerful incentives for trial court judges to follow settled precedent, even if they disagree with it.¹²⁸ Indeed, the burgeoning empirical research on this topic suggests that lower court judges fear reversal as it may harm their reputation and negatively affect their salaries or the likelihood of promotion. In addition, remand decisions create additional, and often duplicative, work for trial court judges.¹²⁹ Even in legal traditions that have no binding precedent, judges tend to deviate from prior appellate court cases only if they have strong reasons to do so.¹³⁰ Lastly, the awareness that a decision may be subject to scrutiny incentivizes first instance judges to draft well-reasoned opinions, as they will try to convince their superiors of the correctness of the position taken. Presumably judges spend more time and

127. Oldfather, *De Novo Review*, *supra* note 1, at 317 (“[A]n appellate court’s correction of an error in any given case tends to foster an environment in which fewer errors are committed in the first instance.”).

128. See Frisch, *supra* note 1, at 85; Shavell, *supra* note 95, at 390–91; but see Caminker, *supra* note 118, at 839–43 (arguing that judicial economy arguments, both from the perspective of lower courts and from the perspective of a legal system, do not provide a full explanation of why lower courts follow precedent). Although arbitrators are not subject to the pressures of potential reversal, outright refusal to apply settled precedent renders their awards vulnerable to vacatur actions or enforcement challenges. See, e.g., *New York Tel. Co. v. Comm’n Workers of Am. Local 1100*, 256 F.3d 89, 91–93 (2d Cir. 2001) (per curiam) (affirming vacatur on the basis of manifest disregard of the law where an arbitrator deliberately refused to apply binding Second Circuit law, stating that “[p]erhaps it is time for a new court decision.”).

129. See Susan B. Haire et al., *Appellate Court Supervision in the Federal Judiciary: A Hierarchical Perspective*, 37 L. & SOC’Y REV. 143 (2003) (empirically testing the principal-agent model of adjudication under which, among other things, trial court judges have relatively strong incentives to avoid reversal by intermediate courts); see also Drahozal, *supra* note 1, at 491–97 (considering the constraining function of the appeals process in holding judicial preferences constant).

130. See, e.g., Olav A. Haazen, *Precedent in the Netherlands*, in PRECEDENT AND THE LAW 227, 235–36 (Ewoud Hondius, ed., 2007) (lower courts in the Netherlands tend to decide in line with higher court decisions); Robert Alexy & Ralf Dreier, *Precedent in the Federal Republic of Germany*, in INTERPRETING PRECEDENTS (D. Neil MacCormick & Robert S. Summers, eds., 1997), at 17, 36 (noting the same regarding Germany); Raj Bhala, *The Myth About Stare Decisis and International Trade Law (Part One of a Trilogy)*, 14 AM. U. INT’L L. REV. 845, 910–15 (1999) (in practice, if not in theory, French courts overwhelmingly follow decisions from higher courts).

resources on opinions that will likely be reviewed on appeal, for example because the stakes are high, or because the case presents important issues of first impression. Moreover, first instance judges will also try to dissuade losing parties from appealing by providing persuasive reasoning in their opinions.¹³¹ The connection between reason-giving and the quality of decision-making, however, is a tenuous one, as judges may use reasoning to mask weaknesses and project conviction even in cases that presented close calls.¹³²

It is a fair question whether many characteristics that account for the quality of decision-making in the appellate courts are already present in the standard single-tier process in international commercial arbitration. After all, in high-stakes international disputes, tribunals typically consist of three arbitrators. The common appointment practices in arbitration, however, offset many of the advantages that come with three-arbitrator adjudication. It has become standard for parties to agree that each party select an arbitrator, and that the two party-appointed arbitrators nominate a chair.¹³³ Compared with the random assignment systems that are used in most courts, parties to arbitrations have tremendous influence over the constitution of the tribunal that will decide their dispute.¹³⁴ To be sure, this is viewed by many as a significant advantage of arbitration, and the institution of the party-appointed arbitrator serves several legitimate goals. A party may want to select an arbitrator who has expertise in the relevant

131. See Mathilde Cohen, *Reason Giving in Court Practice: Decision-Makers at the Crossroads*, 14 COLUM. J. EUR. L. 257, 265–70 (2008).

132. *Id.* at 269 (“Weaknesses of the written reasons enhance the chances of an appeal in matters of law, while skillfully developed reasons may prevent a materially doubtful judgment from being overturned by the court of appeal”).

133. BORN, *supra* note 4, at 1355, 1356, 1403; James H. Carter, *The Selection of Arbitrators*, 5 AM. REV. INT’L ARB. 84, 86 (1994); James Wangelin, *Effective Selection of Arbitrators in International Arbitration*, 14 MEALEY’S INT’L ARB. REP. 69, 70 (1999).

134. For a critical view of random assignment of judges in appellate courts, see Michael Hasday, *Ending the Reign of Slot Machine Justice*, 57 N.Y.U. ANN. SURV. AM. L. 291, 295–98 (2000) (arguing that the random assignment system in appellate courts is unfair to the parties, renders appellate adjudication less predictable and contributes to inter-circuit splits); cf. Mautner, *supra* note 122, at 222 (identifying two sources of “luck” in adjudication: law’s indeterminacy, and the random assignment of judges).

industry or in a specific type of dispute, or who is familiar with that party's legal culture.¹³⁵ Perhaps most importantly, significant party influence on the appointment of a tribunal helps engender confidence in the legitimacy of the process, which in turn may increase compliance with awards.¹³⁶ Yet this appointment practice affects both the incentives of individual arbitrations and the dynamic within the tribunal in ways that present a tension with strict application of the law.

In practice, any attorney worth her fees will try to select an arbitrator who is favorably inclined to the client's position and persuasive to other arbitrators. As bluntly put by Martin Hunter a quarter century ago: "[W]hen I am representing a client in an arbitration, what I am really looking for in a party-nominated arbitrator is someone with the maximum predisposition towards my client, but with the minimum appearance of bias."¹³⁷ Indeed, while party-appointed arbitrators must be impartial, there is some expectation that they will ensure the arguments of "their" side receive sufficient consideration from the tribunal, especially the chair.¹³⁸ The predisposition to

135. See David J. Branson, *American Party-Appointed Arbitrators—Not the Three Monkeys*, 30 U. DAYTON L. REV. 1, 61 (2004).

136. See William W. Park, *Arbitrator Integrity: The Transient and the Permanent*, 46 SAN DIEGO L. REV. 629, 644–45 ("To promote confidence in the international arbitral process, party input into the selection of arbitrators has long been common practice . . . Such party participation democratizes the process, serving to foster trust that at least one person on the tribunal (the party's nominee) will monitor the procedural integrity of the arbitration.").

137. Martin Hunter, *Ethics of the International Arbitrator*, 53 ARB. 219, 223 (1987); see also R. Doak Bishop & Lucy F. Reed, *Practical Guidelines for Interviewing, Selecting and Challenging Party-appointed Arbitrators in International Commercial Arbitration*, 14 ARB. INT'L 395, 396 (noting that most parties follow the guideline that "'their' arbitrators can be generally predisposed to them personally or to their positions, as long as they can ultimately decide the case—without partiality—in favour of the party with the better case."); Christopher R. Seppälä, *Recommended Strategy for Getting the Right International Arbitral Tribunal*, 6 TRANSNAT'L DISP. MGMT. 10 (Mar. 2009) (characterizing as an "essential attribute" for the "party-nominated arbitrator . . . [to] be prepared to consider favorably the case or position of the party nominating him or her."); Wangelin, *supra* note 133, at 70 (noting that the selection of an arbitrator is "guided . . . by the hope of employing one with qualities which tend to give him and his client the greatest assurance that their viewpoint will be understood . . .").

138. See Alan Scott Rau, *Integrity in Private Judging*, 38 S. TEX. L. REV. 485, 497–98 (1997) (describing the role of the party-appointed arbitrators as

ward the appointing party, however slight, may distort the individual deliberation of the party-appointed arbitrators. Indeed, it reduces many of the benefits associated with decision-making by multiple adjudicators. The role of the party-appointed arbitrator, in other words, is at odds with the type of mindset conducive to the prevention of errors: a combination of detachment from the parties and receptiveness to the evidence and arguments presented by both sides.¹³⁹ As a result, even though tribunals in high-stakes commercial arbitration usually consist of three arbitrators, the chair may well end up casting the deciding vote.¹⁴⁰ Yet the presence of two party-appointed

making sure that the chair “fully understands the issues and background of the case, the contentions of each party, and the possible implications of the award before it is issued.”); cf. Andreas Lowenfeld, *The Party-Appointed Arbitrator in International Controversies: Some Reflections*, 30 TEX. INT’L L. J. 59, 65–68 (1995) (“[i]n an international case a party-appointed arbitrator serves as a translator. I do not mean just of language . . . I mean rather the translation of legal culture, and not infrequently of the law itself, when matters that are self-evident to lawyers from one country are puzzling to lawyers from another.”).

139. Legal Realists have offered a powerful critique of this mindset as an idea that is not matched by reality, something Part III.C.1, *supra*, touched on. For purposes of this analysis, what matters is that, *by design*, only one of the three adjudicators in a commercial arbitration panel is expected to even strive to adopt a truly objective a mindset as possible. Cf. Rau, *supra* note 138, at 506–09 (criticizing the notion that international arbitrators can at once be predisposed and impartial, and noting that “[e]ven in the best of circumstances an official rhetoric of ‘independence’ and a tolerated latent ‘sympathy’ must exist in an uneasy tension.”).

140. See Jennifer Kirby, *With Arbitrators, Less Can Be More: Why the Conventional Wisdom on the Benefits of Having Three Arbitrators May Be Overrated*, 26 J. INT’L ARB. 337, 338 (“Contrary to what some parties may believe, the votes of co-arbitrators do not determine any issue to be decided by the arbitral tribunal; rather, it is the vote of the chairman—and only the vote of the chairman—that is ultimately decisive.”); cf. Diane P. Wood, *The Brave New World of Arbitration*, 31 CAP. U. L. REV. 383, 396 (2003) (“Courts have found no fault with the presence of the party-arbitrators on the panel; that system simply focuses attention on the third arbitrator.”). Recognizing the importance of the chair, experienced arbitration practitioners recommend that parties carefully consider the dynamics within the tribunal during the appointment process. See, e.g., Seppälä, *supra* note 137, at 3–4 (“A party’s goal should be the appointment of an arbitral tribunal, a majority (at least) of whose members, while being independent and impartial as regards the parties . . . will at the same time be well disposed towards, or sympathetic to, or at the very least receptive to, that party’s position.”); see also C. Mark Baker, *Advocacy in International Arbitration*, in THE LEADING ARBITRATORS’ GUIDE 381, 384 (Lawrence W. Newman & Richard D. Hill eds., 2008) (noting, as to the selection

arbitrators could influence a chair's ultimate position. As Alan Rau has pointed out, if each of the three arbitrators takes a different view of the outcome, the chair will often negotiate and compromise to reach a majority.¹⁴¹

In addition to the immediate impact of party nomination on particular cases, the private nature of arbitration creates systemic incentives that are at tension with error avoidance. All arbitrators on a tribunal have a strong economic interest in future appointments. Christopher Drahozal has speculated that these market pressures have a constraining influence on arbitrators that is similar to the effect of the possibility of reversal on trial court judges. He suggests that this is a significant reason for the absence of appeals processes from commercial arbitration.¹⁴² Yet, as Drahozal himself has acknowledged, market pressures differ from the constraints on tenured judges, and they may yield different outcomes.¹⁴³ The party-

of a party-appointed arbitrator, "an arbitrator that will remain impartial and independent but understand the advocate's arguments, and who has the right personality to convince the other arbitrators during deliberations, is the ideal choice."); *but see* Kirby, *supra*, at 338 ("[W]hile co-arbitrators may influence the chairman, their influence is often substantially limited by the dynamics within the tribunal, including the chairman's inherent scepticism with respect to anything a co-arbitrator may do that would tend to further the interests of the party that nominated him . . .").

141. Rau, *supra* note 138, at 501 (noting that "[t]he need to obtain a majority often leads to a process of negotiation and compromise, in which the neutral feels obliged to trim or adjust his position in the search for a coalition with one of his colleagues—and ultimately perhaps to concur, reluctantly, in an award different from the one he might have preferred."). Currently, most arbitration rules provide that if no majority can be reached, the chair alone will issue an award. *See, e.g.*, ICC Rules art. 31, ¶1; LCIA Rules art. 26.3; *but see* ICDR Rules art. 26, ¶1 (requiring that decisions and rulings be made by a majority without making provision for the event a majority cannot be reached). Although these provisions give the chair some leverage, there are still institutional pressures and other incentives for a chair to try to reach consensus or at least a majority, as such a result increases the appearance of legitimacy of the process and the decision.

142. Drahozal, *supra* note 1, at 501–02; *see also* Shavell, *supra* note 95, at 424 (noting that "because parties select their arbitrators, arbitrators have an economic interest in not making errors and in maintaining their reputation. Judges do not have a similar interest.").

143. Christopher R. Drahozal, *Privatizing Civil Justice: Commercial Arbitration and the Civil Justice System*, 9 KAN. J. L. & PUB. POL'Y 578, 588 (2000) ("Arbitrators compete with each other to be selected. You don't have similar market competition in the judiciary.").

appointed arbitrator's incentive is to achieve a resolution that is satisfactory to the side that nominated him or her.¹⁴⁴ In a perfectly balanced situation, the chair—who wants to obtain future appointments from either or both of the parties—is motivated to resolve the dispute in a way that is acceptable to both sides. In many instances, however, one of the parties will be more likely than the other to nominate the chair in the future. One party may likely go out of business, or maybe the arbitrator has expertise in a niche area in which one of the parties specializes. Perhaps one party is represented by a leading practitioner who frequently advises clients with regards to appointments. The chair, in other words, is not always unaffected by the practice of party-appointment. Furthermore, even if the tribunal's incentives cancel each other out, the desire to reach a resolution with which both sides can live should not be equated with rigorous application of legal standards.¹⁴⁵ To understand why, one need only imagine a judge who is incentivized to reach a decision that gives something to each party, rather than considering herself constrained to deter-

144. See Alan Scott Rau, *The Culture of American Arbitration and the Lessons of ADR*, 40 TEX. INT'L L.J. 449, 459 (2005) (noting that "it [cannot] escape even the most ingenuous of arbitrators that he is rather more likely to be nominated again by someone who has already been willing to nominate him once."). Recently, other well-respected arbitrators have advocated for abolition of party-appointment to put an end to these incentives and ensure true impartiality. See generally Jan Paulsson, *Moral Hazard in International Dispute Resolution: Inaugural Lecture*, University of Miami School of Law (Apr. 10, 2010), 8 TRANSNAT'L DISP. MGMT., no. 2, 2011; Hans Smit, *The Pernicious Institution of the Party-Appointed Arbitrator*, Columbia FDI Perspectives (Dec. 14, 2010), available at <http://www.vcc.columbia.edu/content/pernicious-institution-party-appointed-arbitrator>. Unsurprisingly, these proposals have been met with resistance. See, e.g., Herman Manuel Duarte, *Fixing the Way Multi-Arbitrator Tribunals Are Formed*, ABA Section of Litigation (Oct. 27, 2011), available at <http://apps.americanbar.org/litigation/committees/international/articles/fall2011-multi-arbitrator-tribunals-unilateral-appointments.html>; Alexis Mourre, *Are Unilateral Appointments Defensible? On Jan Paulsson's Moral Hazard in International Arbitration*, Kluwer Arbitration Blog (Oct. 5, 2010), available at <http://kluwerarbitrationblog.com/blog/2010/10/05/are-unilateral-appointments-defensible-on-jan-paulsson%E2%80%99s-moral-hazard-in-international-arbitration>.

145. Cf. Christopher R. Drahozal, *Is Arbitration Lawless?*, 40 LOYOLA L.A. L. REV. 187, 192 (2006) ("If faced with a choice between a decision preferred by the parties or one that follows the law, arbitrators have an incentive to choose the former.").

mine the outcome based on the merits of the parties' positions.

To be sure, arbitrators have a long-term interest in developing a reputation for fairness and accuracy.¹⁴⁶ Yet arbitrators may be more prone than judges to creativity, especially when a strict approach seems to result in an unjust or impractical outcome.¹⁴⁷ In part, this is because arbitrators are not burdened by the constraints that come with responsibility for the development of a body of substantive law. The private, contractual nature of arbitration thus facilitates flexible application of the selected laws.¹⁴⁸ One last check on judges that is mostly lack-

146. Cf. Rau, *supra* note 144, at 514–15 (“Now I imagine it is fair to say that arbitrators usually do try their best to model their awards on what courts would do in similar cases—and that as often as not they succeed in doing so. . . . Above all perhaps, arbitrators may be expected to act in such a way as to maximize the likelihood that their awards will be enforceable in all jurisdictions where review is likely . . .”).

147. Alan Rau provides some specific examples in which arbitrators reach results that are sensible from a business perspective, but cannot easily be squared with legal doctrines. Rau, *supra* note 138, at 533–34. For example, in a strong claim for rescission of a joint venture agreement for fraud, if a tribunal believes that the claimant is partly to blame in connection with reliance, the tribunal could justify reduced recovery based on an analogy to comparative negligence doctrines. *Id.* (citing John E. Coons, *Approaches to Court Imposed Compromise—The Uses of Doubt and Reason*, 58 NW. U. L. REV. 750, 768 n.12, 774–75 (1964)); see also CPR COMM’N ON THE FUTURE OF ARB., COMMERCIAL ARBITRATION AT ITS BEST: SUCCESSFUL STRATEGIES FOR BUSINESS USERS 270–71 (Thomas J. Stipanowich & Peter H. Kaskell, eds., 2001) (citing court decisions recognizing that arbitrators have more leeway than judges in fashioning remedies and may, for example, order specific performance). Some commentators suggest that arbitrators’ leeway extends beyond remedies. See, e.g., Hans Smit, *Contractual Modifications of the Arbitral Process*, 113 PENN ST. L. REV. 995, 1006 (2009) (“Arbitrators have desirable leeway in developing and applying law to fit the circumstances of the individual case . . .”); Stephen J. Ware, *Default Rules from Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 725 (1999) (“[A]rbitrators often do not apply the law”); cf. Kaufmann-Kohler, *supra* note 15, at 364 (“[A]rbitrators have an inclination to ‘transnationalise’ the rules they apply, either because they are subject to no meaningful controls when it comes to the merits, they act in a transnational environment, or they are themselves very often from different legal cultures.”).

148. Cf. Paul D. Carrington & Paul H. Haagen, *Contract and Jurisdiction*, 1996 SUP. CT. REV. 331, 346 (noting that “[e]ven [ICC] arbitrators are dependent for their careers, to a degree that no judges are, on the acceptability of their awards to the parties, and perhaps especially on their acceptability to parties who are ‘repeat players’” and suggesting that for “[f]or this reason . . . reluctant parties have cause to believe that their legal entitle-

ing in arbitration is the court of public opinion. In contrast with judges, who must open their courtrooms to the public and the press and whose opinions are published, commercial arbitrators operate in relative obscurity.¹⁴⁹ Of course, they are scrutinized by their fellow arbitrators, as well as the parties and their counsel. Yet the pressures created by interactions with those who are immediately involved in the arbitration are different from those that result from the possibility of evaluation by a broader public.

In sum, combined with other characteristics of arbitration, the direct appointment of arbitrators by the parties creates incentives that are at odds with error correction. Appellate review in commercial arbitration can therefore be effective only if parties and institutions are willing to use another appointment model for the appellate panel. Of course, so long as the party-appointed arbitrator remains a fixture in arbitration, even arbitrators on tribunals that are selected in their entirety by an institution have incentives that are different from those of tenured judges. But at least the immediate effect of party-appointment would be reduced.

D. *Error Correction in Commercial Arbitration*

Having analyzed the conditions for error correction, we are now in a position to assess whether this value should be implemented in international commercial arbitration. This section addresses the question in three steps. It explains, first, why the rules of arbitration institutions are the most appropriate vehicles for the implementation of error correction. It then identifies some features a two-tier process should have in

ments will be more squarely observed in court than in an arbitral tribunal . . ."); see also Rau, *supra* note 144, at 515 n.271 (discussing Carrington and Haagen's statements about incentives of arbitrators, and observing that these incentives are consistent "with our recognition of the truism that the primary felt obligation of the arbitrators is at all times to the contracting parties rather than to the state").

149. Knull & Rubins, *supra* note 2, at 541 n.31 ("[J]udges, as public figures, are more concerned about the effect each decision will have upon their reputation than arbitrators, who enjoy some degree of anonymity."). Eric Posner has argued that the possibility of substantive review of arbitral awards by national courts creates an incentive for arbitrators to engage in more diligent decision-making. Eric A. Posner, *Arbitration and the Harmonization of International Commercial Law*, 39 VA. J. INT'L L. 647, 651-52, 667 (1999).

order to achieve meaningful error correction within the arbitration framework. Lastly, it discusses the normative question of whether institutions *should* make an appellate option available, or at least experiment with it.

1. *The Nature of Arbitration Rules*

At the outset, let me emphasize that arbitration in a single instance offers significant advantages and that it works for many parties who avail themselves of arbitration. Any proposal for appellate review in international commercial arbitration should therefore not be mistaken for a call to revolutionize the arbitration process or to spring a highly unconventional process on unsuspecting parties. The common practices will continue to be the default. This raises the question of whether we shouldn't simply leave it to the parties themselves to come up with tailor-made appeals processes. After all, they are free to agree to appellate review, either by supplementing the selected arbitration rules (which, consistent with the consensual nature of arbitration, tend to be default rules), or by opting for arbitration outside the arbitration institutions.

Yet few parties will make the effort. In part, this is because many parties do not give the nuts and bolts of arbitration extensive thought at the time they agree to it. The arbitration provision is typically negotiated along with the substantive terms of a complex transaction, at a time when no dispute is on the horizon. Another complication is that appellate review only makes sense for certain disputes. Although parties could specify under which circumstances a right to appeal exists (e.g., when the amount in dispute or the damages awarded reach a certain threshold), few arbitration clauses go into this level of detail. More generally, the transaction costs of requiring parties to negotiate and document the specific features of an appeals process are significant, and the result probably will not be optimal. After a dispute has materialized, it is even less likely that the parties will hammer out an agreement specifying a detailed two-tier arbitration process.

The parties' freedom to adjust the arbitration process to their needs has prompted the suggestion that arbitration institutions should provide a menu of options regarding critical

features of a two-tier process.¹⁵⁰ But the value arbitration institutions can provide, aside from their roles in appointing arbitrators and facilitating logistical aspects of the proceedings, lies in their ability to develop default procedures that are sensible to most parties. When an arbitration institution issues a new set of rules, it should be able to offer a principled defense of the choices it has made. Of course, some parties will wish to deviate from the rules, and institutions should generally enforce arrangements that do not present blatant challenges for enforceability, for example, by violating fundamental notions of impartiality and due process.¹⁵¹ Institutions would do their customers a disservice, however, by simply presenting the parties with a menu of choices that would require extensive analysis, followed by negotiation about each item.¹⁵² Instead, if institutions offer appeals processes, these should satisfy a substantial portion of those parties who would wish to opt into a two-tier process.

2. *Achieving Error Correction*

What follows is the outline of a proposed two-level arbitration system that would create conditions conducive to error correction, in the sense of meaningful review of an initial award and improvement of the quality of adjudication in first instance.¹⁵³ Some features of the proposed process will render the arbitration process more similar to litigation. At the same

150. See *supra* note 90 and accompanying text for a description of such a proposal.

151. Cf. Craig, *supra* note 15, at 282 (noting that there is no absolute duty on arbitrators to render an enforceable award, but they are under an obligation to use their best endeavors to do so).

152. In similar vein, Hans Smit has noted with regards to the appropriate scope of review for an appellate arbitral panel: "The considered judgment of the drafters of institutional and ad hoc rules as to the most desirable scope of review is likely to be better than ad hoc determinations by drafters of contracts who are unlikely or unable to give the question the consideration it deserves." Smit, *supra* note 147, at 1005. Smit considers the possibility that rules governing appellate arbitral review provide a preferred option as well as possible alternatives, but notes that if there are strong institutional interests in providing a single option, the rules should specifically exclude provision for a different scope of review. *Id.* at 1005–06.

153. I will not discuss features that are important from an arbitration-technical perspective, but do not go directly to the error correction function, such as provisions to address the lack of finality of the first award if an appeal is taken, or disincentives that could be created by cost provisions (for exam-

time, the process differs in some respects from the court model so as to accommodate features of the arbitration process.

Number of Arbitrators. The first feature of the proposed two-level arbitration process may seem self-evident, but it requires a drastic change from current practice: The first instance arbitration should be conducted by a sole arbitrator, and the appellate procedure by three arbitrators.¹⁵⁴ This is important, not only for reasons of efficiency, but because an increase in the number of adjudicators is a critical condition for the effectiveness of review for error. The absence of hierarchy in commercial arbitration already renders the concept of error correction problematic. If one accepts that three adjudicators will reach a better result than one, however, it is at least plausible that the second tribunal will reach a better decision even if the sole arbitrator is no less qualified than any member of the appellate panel. Moreover, because of their experiences with court systems, parties would be more likely to accept an appellate tribunal's reversal or modification of an earlier award that is rendered by only one arbitrator.¹⁵⁵

ple, an asymmetrical provision under which the party that files an appeal is liable for the costs of the other party if it loses).

154. Arbitration agreements usually specify the number of arbitrators, with most opting for a three-member tribunal. *See* Wangelin, *supra* note 133, at 72–73 (“Procedurally, it is typical that the party-appointed arbitrators select the chairman or presiding arbitrator. . . . The practitioner . . . will want the process to allow him freely to suggest candidates known to be acceptable to his client and to object to candidates proposed by the opposition.”). Most arbitration rules, including those of institutions that have adopted appellate procedures, provide for a sole arbitrator as a default. They also note, however, that a dispute will be submitted to three arbitrators if the parties so agree or if the appointing authority concludes that would be more appropriate. *See, e.g.*, ICC Rules art. 12, ¶2; ICDR Rules art. 5; LCIA Rules art. 5.4. In practice, institutions tend to appoint three arbitrators if the amount in dispute exceeds a certain threshold amount. *See, e.g.*, MICHAEL W. BÜHLER & THOMAS H. WEBSTER, *HANDBOOK OF ICC ARBITRATION* 139 (2005) (“For arbitrations where the amount in dispute is over US\$ 10 million, one would generally expect the ICC Court to decide that there should be a tribunal of three arbitrators.”).

155. It would be less ideal to go from three arbitrators in the first instance to five on appeal. Although the logic underlying the Condorcet jury theorem compels the conclusion that five minds are even better than three, the improvement is relatively marginal and comes at significantly increased expense and longer delays. Moreover, because the added value is less dramatic, parties are less likely to accept an award from a five-member panel

Appointment of the Appellate Tribunal. As we have seen, the incentives created by the institution of the party-appointed arbitrator are incompatible with error correction. Therefore, the appellate tribunal should either be selected by agreement of both parties or, more realistically, by the arbitration institution.¹⁵⁶ The proposed practice would reduce one of the features of arbitration that is most valued by parties, namely significant control over the selection of the adjudicators. Yet institutions could still solicit input from the parties, so long as there is no direct appointment link between a party and an arbitrator.¹⁵⁷ For example, the parties may agree on some qualifications (or, if they cannot agree, to submit a description to the institution without sharing it with the other side). The institution could also give the parties a preliminary list of potential arbitrators, which they must return with a ranking and a limited number of “strikes.” Adoption of a list procedure, which in some form or other has been followed by a number of institutions including the AAA, would significantly reduce distortions caused by the party-appointed arbitrator system. At the same time, it would leave the parties with some influence and, importantly, the ability to veto “rogue” arbitrators.

Lastly, even though the joint appointment of three arbitrators may be unrealistic in most cases, there is a greater likelihood that parties will be able to identify one arbitrator who is acceptable to both sides. In fact, the possibility of substantive review may take some of the pressure off the appointment of the first instance arbitrator, making it easier for the parties to reach agreement. In practice, therefore, the parties would maintain a high level of control over the appointment of the first instance arbitrator.

that overturns a decision from three-member panel, especially if the appellate panel is divided. In sum, going from one to three adjudicators seems the best model for error correction.

156. Hans Smit has argued that, in light of the importance of the constitution of an appellate tribunal, its members should be appointed by the supervising arbitration institution or a third party (in practice, also a leading arbitration institution). See Smit, *supra* note 147, at 1007.

157. Another solution would be one in which parties nominate arbitrators, but the arbitrators do not learn which party appointed them. Realistically, however, in the relatively small, closely knit community of elite international arbitration practitioners, arbitrators would often be able to make an educated guess as to which side appointed them.

Standard of Review. This factor is critical, as the level of deference due to the first award determines the scope of the appellate tribunal's error correction mandate. The existing arbitral appeals procedures demonstrate three notions of what appellate review could accomplish. On one end of the spectrum is CPR's standard, under which appellate panels may overturn an award that "does not rest upon any appropriate legal basis" or that "is based upon factual findings clearly unsupported by the record[.]"¹⁵⁸ On the other end is the European Court of Arbitration, which provides for *de novo* review on both factual and legal determinations. JAMS, by providing that the appellate panel adopts the standard of review that would be used by appellate courts in the jurisdiction in which it sits, does not take a position. CPR's highly deferential standard appears to be primarily concerned with the promotion of a fair arbitration process in the first instance.¹⁵⁹ This level of review may be satisfactory for parties who wish to obtain a safeguard against arbitrary or capricious awards. Yet parties who wish to optimize the error correction function will benefit from a more searching review of the first instance award.¹⁶⁰ In other words, a *de novo* standard of review is the most appropriate one for errors of law.

The standard of review for facts is a more controversial subject, as it is one area in which the practices of court systems in different jurisdictions show significant variation. In light of the nature of international contractual disputes and the characteristics of the arbitration process, *de novo* review of facts would appear to be appropriate. For one, it is often hard to draw the line between law and facts in cases involving the in-

158. CPR Rules of Appeal Procedure, r. 8(2).

159. See Martin Shapiro, *Appeal*, 14 L. & Soc'y REV. 629, 629 (1980) (identifying as the "principal purpose" of appellate review, from the perspective of the losing party, "to protect the loser against an arbitrary, capricious, or mistaken decision by the trial judge"); cf. CARRINGTON ET AL., *supra* note 1, at 2 ("[T]he review for correctness serves to reinforce the dignity, authority, and acceptability of the trial, and to control the adverse effects of any personal shortcomings of the basic decision-makers.").

160. Cf. Lord Justice Dyson, *The 2000 Eversheds Lecture: Finality in Arbitration and Adjudication*, 66 ARB. 288, 288 (2000) (noting that "the more generous the scope for challenging decisions by appeal or review, the greater the chance of eliminating error.").

terpretation and application of complex agreements.¹⁶¹ More fundamentally, there is no reason to believe that the notion that three adjudicators are likely to reach better decisions does not apply to questions of fact.¹⁶² As noted above, the systemic choice to focus appellate resources on lawmaking provides a significant explanation for the existence of two distinct standards of review in the United States. Appellate courts in Europe, which do not play as prominent a role in lawmaking, have authority to review all aspects of the case from which appeal is taken. Since the implementation of appellate review in international commercial arbitration would be justified exclusively in terms of error correction, much of the justification for a different treatment of questions of fact and law would appear to fall away.

The case for full factual review faces at least two objections. The first objection is that a certain distance from the fact-finding process allows appellate decision-makers to reach better decisions on legal issues. It may result in greater objectivity.¹⁶³ Relatedly, a renewed focus on facts arguably would diminish the attention appellate adjudicators can devote to legal issues.¹⁶⁴ These arguments have some force with regards to novel legal issues. They are less apt, however, in the context of appeals that center on the correct application of legal standards to complex or disputed facts, which would describe the nature of adjudication in many international commercial disputes. More importantly, while it may be sensible in a legal

161. See Randall H. Warner, *All Mixed Up About Contract: When Is Contract Interpretation a Legal Question and When Is It a Fact Question?*, 5 VA. L. & BUS. REV. 81 (2010) (describing different approaches in determining whether contract interpretation involves questions of fact or law, and claiming that the answer depends on the nature of the contract at issue).

162. Cf. GORDON TULLOCK, TRIALS ON TRIAL 166–67 (1980) (“If we are going to have an appellate procedure . . . and we do think that it improves the quality of ‘justice,’ then there does not seem to be very much argument for not allowing appeals on every aspect of the case[.],” including findings of fact).

163. Cf. Carrington, *supra* note 118, at 551 (noting that “[r]emoteness of the reviewer from the firing line of trial can assure greater objectivity for the institutional process.”).

164. Cf. Martin B. Louis, *Allocating Adjudicative Decision Making Authority Between the Trial and Appellate Levels: A Unified View of the Scope of Review, the Judge/Jury Question, and Procedural Discretion*, 64 N.C. L. REV. 993, 1013 (1986) (“To provide free review of ultimate facts, appellate courts would have to steal the necessary additional time from the law-declaring function . . .”).

system to sacrifice, within limits, accuracy in fact-finding in favor of better decision-making on legal issues, the justifications for this tradeoff are significantly weaker when the law-making function is absent.

The second objection is that *de novo* review of facts is inefficient.¹⁶⁵ While the examination of witnesses on appeal inevitably would add time and expenses, these costs are to some extent mitigated by common arbitration practices. For instance, in international commercial arbitration cases parties often submit signed witness statements in lieu of live testimony. Moreover, key witnesses who testify at a hearing are often only subjected to targeted questions from opposing counsel and the tribunal.¹⁶⁶ This said, the tension between error correction and efficiency is a real one. Even in court systems, error correction gives way to other considerations, as we have seen in the case of the legal system in the United States in which appellate courts have limited authority to review for factual errors. Similarly, arbitration institutions and parties may balance these interests differently.

One way to increase efficiency could be to videotape the hearings in the first instance arbitration and agree that on appeal, the parties will only use transcript excerpts in their written submissions and recorded segments at the hearing. The appellate arbitrators could be given the authority to call witnesses if they believe additional testimony is likely to clarify key issues that were not sufficiently addressed in the first instance proceeding. Alternatively, parties could limit the first instance arbitration proceeding to paper submissions, with a brief hearing, possibly conducted by telephone or videoconference, at which counsel can be heard, and perhaps a limited number of key fact and expert witnesses. If it comes to an appeal, the parties would have the opportunity to make supplemental submissions. The second level arbitration would also be the opportunity for the parties to present witnesses so that three arbi-

165. See, e.g., Marrow, *supra* note 73, at 12 (proposing that any arbitral appeal be limited to issues of law to safeguard some of the expediency and cost-effectiveness of arbitration).

166. See, e.g., Gabrielle Kaufmann-Kohler, *Globalization of Arbitral Procedure*, 36 VAND. J. TRANSNAT'L L. 1313, 1329–30 (2003) (describing this practice and explaining how it represents a hybrid between the common law trials, with its emphasis on live witness testimony, and civil law trials, in which documents play a larger role).

trators, rather than one, can make determinations of credibility based on demeanor. Both proposed alternatives to two full-blown trials would still provide many of the benefits associated with error correction. In particular, several aspects relating to the improvement of the quality of adjudication are preserved. The second-level arbitrators and the parties would have the benefit of a reasoned first instance determination to focus their attention on the most critical issues. Both processes would also maintain the constraining influence on the first instance arbitrator that comes from the awareness that a panel of three peers may soon be poring over the award.

Each of the two alternatives to a full hearing at each level has distinct advantages and drawbacks. The first alternative makes more factual information available to the first instance arbitrator. This increases the likelihood that the award rendered by the first arbitrator is compelling to the losing party, and makes appeal less likely. The availability of the backstop of appellate review, ironically, would convince parties to place greater trust in a sole arbitrator. Another advantage is that this solution would prioritize the process before an arbitrator jointly selected by the parties (if they reached agreement on the first instance arbitrator). It is especially effective when the parties appoint an experienced arbitrator. This solution may strike the best balance between the competing interests of accuracy, diligence and efficiency. Yet the second alternative offers some advantages over the first. It may seem strange to place a stronger fact-finding task with the appellate tribunal and to ask the first instance arbitrator to rule on more limited information, increasing the likelihood of error at that stage. It is noteworthy, however, that arbitrators are not required to adopt the relatively "passive" attitude of judges in common law systems. An arbitrator has the power to request more information or clarification on legal or factual issues.¹⁶⁷ Moreover, streamlined processes are not unheard of even in court systems. Instead of conceiving of first-level arbitration as a trial, one could think of it as something akin to a preliminary injunction hearing in the United States. Another, perhaps bet-

167. See, e.g., Park, *supra* note 17, at 35 (describing the international arbitration process as a combination of the common law and civil law approaches, and noting that arbitrators tend to adopt an inquisitorial style with regards to witness testimony).

ter example is the so-called “*kort geding*” in the Dutch courts.¹⁶⁸ This summary proceeding was designed as a means to obtain interim relief in urgent matters, but in the vast majority of the cases the parties do not proceed to a full process after obtaining a decision.¹⁶⁹ Thus, appellate review may be more likely in the second alternative, but it is by no means inevitable. In fact, limitations on the collection and submission of evidence may simply result in a stronger focus on the most important aspects of a case.¹⁷⁰ The second solution would also sidestep some of the problems posed by the concept of “error” in complex contracts cases. Rather than assessing whether the determination made by the sole arbitrator is within the range of acceptable answers, the second panel would take full responsibility for review of the case and reach a decision that is independent from, but also aided by, the first instance arbitrator’s findings.

168. The proceeding, which is conducted by the president of the trial court, is informal and usually requires only one hearing. The president often provides an initial assessment of the case during the hearing, and parties often settle at that stage. Erhard Blankenburg, *Patterns of Legal Culture: The Netherlands Compared to Neighboring Germany*, 46 AM. J. COMP. L. 1, 24 (1998).

169. See Xandra E. Kramer, *Dutch Private International Law—Overview 1998–2002*, 22 Praxis des internationalen Privat-und Verfahrensrechts 537, 546 n.73 (2002) (only about five percent of *kort geding* cases are followed by a full proceeding); see also Heleen Sprenger, *Latest Developments in Cross-Border Litigation: Discovery and Injunctive Relief—the Dutch Perspective*, 11 Int’l L. Practicum 101, 102 (1998) (noting that “in practice *kort geding* proceedings replace the actual substantive proceedings”). The popularity of *kort geding* is probably in large part due to its expediency: decisions are usually rendered within a few weeks, sooner if needed, whereas a full proceeding takes, on average, a year and a half. Kramer, *supra*, at 546 n.73.

170. Geoffrey Miller has proposed to introduce “preliminary judgments” into U.S. civil procedure. Under his proposal, at any time during the litigation, a party could seek a preliminary judgment (which can be vacated by the losing party) on the entire case or on discrete aspects of the case. Geoffrey P. Miller, *Preliminary Judgments*, 2010 U. ILL. L. REV. 165, 168–69. He argues that even though the likelihood of error increases when a court rules on limited information, this risk should not be overstated as in many cases a judge will be able to make a reasonable assessment when some discovery has been done. He also points out that underdeveloped records are often a problem in contexts in which judges provide assessments of the merits before trial, but that it is tolerated in those contexts, and that judges and parties accept the provisional character of such judgments. *Id.* at 171–72.

3. *Should Arbitration Institutions Offer Appeal?*

Now that we have seen what error correction in commercial arbitration could look like, the time has come to address the ultimate question: Should institutions adopt such a process? In the context of contractual, privately funded adjudication, this question breaks out into two parts. First, would the addition of an appeals procedure improve the arbitration process? Second, is there sufficient interest among users and potential users of the arbitration process?

As to the first question, the most obvious objection is that a two-tier process would insert unnecessary inefficiency into arbitration. Even if most parties would not opt in, one could argue that by offering rules for such a process an institution would lend legitimacy to a process that may well result in additional delay and costs for no good reason. This concern is in line with the complaint that international arbitration already suffers from “judicialization,” i.e., the loss of distinct arbitration characteristics as a result of the adoption of court-like features.¹⁷¹ Yet it bears emphasizing that the process would be entirely optional. Since the majority of current arbitration users are relatively content with the status quo, it is unlikely that the two-tier process would effectively come to replace current practices. Moreover, for many parties the two-level arbitration process outlined above may prove to be *more* efficient than the current system. Some parties will accept the award from the first arbitrator. I suspect that more commonly, parties will use the receipt of the first award as a logical moment to engage in serious settlement discussions. The award gives parties more insight into the strength of their legal positions and the potential value of their claims. At the same time, the risk that a second tribunal may arrive at a different conclusion will leave the winning party with incentives to reach a compromise, especially when the award appears to be weak on certain points.¹⁷² From the perspective of parties to commercial dis-

171. See, e.g., Alan Redfern, *Stemming the Tide of Judicialisation in International Arbitration*, 2 *WORLD ARB. & MEDIATION REV.* 21, 21, 24 (2008).

172. A recent survey found that under the current system, at least forty percent of the corporations involved in arbitration cases negotiated a settlement after an award was rendered (the actual number is likely higher, because only thirty percent responded that they did not renegotiate arbitral awards, and thirty percent indicated they did not know). The main reasons

putes, after all, adjudication is not only or even primarily about the vindication of justice. It is also about risk. By extending the timeframe in which each party has something to lose, the possibility of appellate review would affect the dynamics in negotiations that often take place in the shadow of the arbitration process.

A related objection is that much of what my proposal seeks to accomplish could be achieved by abolishing direct party appointment. In other words, the more efficient and less radical solution would be for institutions to change the default rule regarding appointment of the tribunal so that arbitrators are selected by the institutions. In fact, the LCIA already has adopted this approach.¹⁷³ Yet this solution, while removing the incentives created by direct party appointment, fails to offer some of the benefits associated with appellate review. Most obviously, a panel of three arbitrators can still make errors, and there would be no avenue for recourse. The parties also would not have the benefits that stem from an arbitrator's awareness that her award may well be reviewed. In sum, institutional appointment of arbitrators has some advantages over direct party-nomination of the majority of a tribunal, but the solution would not provide many benefits associated with error correction.

This leaves the question of whether a market exists for an appeals process in international commercial arbitration. In an article published about thirty years ago, William Landes and Judge Richard Posner posited that the virtual absence of appellate review in commercial arbitration is simply a consequence of the circumstance that commercial arbitrators don't make law. They stated that the lack of appeals options in commercial arbitration "suggests that the principal value of appel-

for entering into negotiations after an award is obtained are avoidance of cost (thirty-three percent), saving time associated with enforcement (twenty-three percent), preservation of a continuing relationship with the other side (nineteen percent) and the desire to receive the funds promptly (sixteen percent). Queen Mary University of London & PricewaterhouseCoopers, *International Arbitration: Corporate Attitudes and Practices*, 9 (2008), available at http://www.pwc.co.uk/eng/publications/international_arbitration_2008.html.

173. See LCIA Rules art. 5.5 (arbitrators are appointed by the LCIA court, which pays due regard to any written agreements about selection methods or criteria).

late proceedings is not to correct errors at the trial level but to formulate rules of law.”¹⁷⁴ The underlying premise is that private parties are unwilling to pay for error correction, but that a legal system as a whole will pay for rule creation. On the other hand, the intermediate appellate courts in the federal court system of the United States were created primarily to correct errors made by trial courts.¹⁷⁵ And as we have seen, in many jurisdictions, especially in the civil law tradition, appellate courts still engage principally in error correction. In commercial arbitration, the absence of external checks on tribunals—either through appellate review or through the norms of openness and transparency that apply to court proceedings and decisions—increases the risk of a decision that exceeds the parameters imposed by the parties’ contracts, including any choice of law provisions. Thus, although the absence of a broader rule-setting responsibility takes away a significant justification of the costs and inefficiencies that come with appellate review, in bet-the-company cases it may be a price worth paying. For parties who place a premium on diligent decision-making over the benefits of obtaining a speedy and final resolution, it may be sensible to provide for the possibility of obtaining a check on the first instance tribunal.

The available data is inconclusive regarding the potential demand for an appeals process. According to a survey of 606 in-house attorneys from Fortune 1,000 corporations con-

174. William M. Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 J. LEGAL STUD. 235, 252 (1979). Kenneth Scott has also argued that the dispute resolution model offers no justification for appeal: “The position that appeals are never essential draws intellectual support from the Conflict Resolution Model. In terms of a mechanism for settling disputes, one hearing is enough to do the job, and it is all that arbitration and grievance procedures customarily afford. No doubt the loser would like another chance, but that it endlessly true. Rather than the outcome it is the existence of a form of impartial arbitrament that is essential.”). Kenneth E. Scott, *Two Models of the Civil Process*, 27 STAN. L. REV. 937, 946 (1975).

175. See, e.g., Paul D. Carrington, *The Function of the Civil Appeal: A Late-Century View*, 38 S.C. L. REV. 411, 416 (1987) (noting that the vision underlying the passage of the Evarts Act was that the law “was presumed clear and, thus, amenable to application.”); Martha Dragich, *Uniformity, Inferiority, and the Law of the Circuit Doctrine*, 56 LOY. L. REV. 535, 560 (2010) (noting that in passing the Evarts Act “Congress was focused primarily on the need for increased capacity for error correction . . . [although] the Act’s sponsors were concerned with uniformity of decisions under federal law.”); see also Oldfather, *Error Correction*, *supra* note 1, at 65 (citing Carrington’s article).

ducted in 1998, 54.3 percent of respondents who did not opt for arbitration indicated that the difficulty of appealing arbitration awards was a major factor in their decision.¹⁷⁶ This group does not consist solely of businesses that categorically reject arbitration: Of the respondents who use arbitration very frequently or frequently, forty-nine percent and sixty-four percent, respectively, indicated that in instances in which they decide against it, the lack of substantive review is a factor.¹⁷⁷ Based on this data, Knull and Rubins conclude that “[b]y not offering appeal options, arbitral institutions ignore an opportunity to respond to needs felt by some potential users.”¹⁷⁸ A survey conducted by PricewaterhouseCoopers (PwC) and the Queen Mary University of London in 2006, however, found that out of 103 in-house counsel of “leading corporations around the world,” ninety-one percent of respondents rejected the idea of an appeals system in international arbitration.¹⁷⁹

176. David B. Lipsky & Ronald L. Seeber, *The Appropriate Resolution of Corporate Disputes: A Report of the Growing Use of ADR by U.S. Corporations* 8, 26 (1998), available at <http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1003&context=icrpubs>; Knull & Rubins, *supra* note 2, at 532 (quoting Lipsky and Seeber).

177. Lipsky & Seeber, *supra* note 176, at 27–28.

178. Knull & Rubins, *supra* note 2, at 534. A study conducted by Theodore Eisenberg and Jeffrey Miller, which examined over 2,800 contracts filed with the Securities Exchange Commission in 2002 by public firms, found that although arbitration agreements were twice as common in international contracts as in domestic ones, only twenty percent of international contracts had an arbitration clause. Theodore Eisenberg & Jeffrey P. Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 DEPAUL L. REV. 335, 351–52 (2007). Although the study is not focused on commercial contracts, its findings challenge the conventional wisdom that arbitration is the dispute resolution mechanism of choice for parties to international transactions. Arbitration experts have proffered significantly higher estimates for commercial transactions, with some placing the estimate as high as ninety percent. Gary Born thinks this number is inflated, but notes: “It is probably true that, in negotiated commercial (not financial) transactions, where parties devote attention to the issue of dispute resolution, and where the parties possess comparable bargaining power, arbitration clauses are more likely than not to be encountered.” BORN, *supra* note 4, at 71.

179. QUEEN MARY UNIVERSITY OF LONDON & PRICEWATERHOUSE COOPERS, INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2, 15 (2006), available at http://www.pwc.co.uk/eng/publications/International_arbitration.html. The PwC survey does not specify which companies were surveyed or what the response rate was. The inconsistency with the Lipsky & Seeber study, *supra* note 176, possibly reflects a selection bias, i.e., attorneys

Attorneys who participated in interviews explained that they would view the ability to appeal as a disadvantage, and they considered finality and the attendant efficiency to be an advantage of the arbitration process.¹⁸⁰ An important lesson from the PwC survey is that even in the international context, users of the arbitration process value efficiency. There is a reasonable possibility that more in-house counsel would opt for an arbitration process that includes an option to appeal if it is designed so as to minimize inefficiency.

It is therefore hard to predict the level of interest for the two-level procedure outlined above. At least initially, most arbitration users will probably prefer arbitration as they know it: in a single proceeding before a three-member tribunal that includes two party-appointed arbitrators. Even if sufficient interest develops, some amount of time will pass before parties consider adopting the “new” procedure in arbitration agreements. Of course, parties are free to opt for the new procedure after a dispute has arisen. To test whether an appellate option adds value, an arbitration institution could pilot the proposal for a few years. At the outset of the arbitration proceeding, it could offer parties a set of rules providing for a two-level procedure as an alternative to its regular arbitration procedure. The institution should closely monitor arbitrations conducted in accordance with the alternative procedure and keep detailed records of the percentage of cases in which parties, respectively, comply with the first award, settle the dispute after the first award, settle the dispute during the appeals procedure, or proceed all the way through the second stage. It should also keep track of how many appellate awards lead to enforcement proceedings, compared to awards in regular arbitration proceedings.

Ultimately, the question of whether international commercial arbitration should make error correction available goes to the heart of what adjudication is about. For many parties, the ability to nominate one of the arbitrators and exert

who had good experiences with arbitration may have been more likely to respond to the PwC survey.

180. QUEEN MARY UNIVERSITY OF LONDON & PRICEWATERHOUSE COOPERS, *supra* note 179, at 15; *see also* BORN, *supra* note 4, at 82 & n.472 (citing the 2006 PwC survey, *supra* note 179, and noting that, on balance, most businesses regard the efficiency provided by finality favorably).

influence over the identity of the chair is a significant advantage of arbitration.¹⁸¹ At the end of the day, many parties may prefer the efficiency that comes with a one-shot process and a certain level of control over the appointment of the tribunal. Some parties may view the freedom of arbitrators to fashion resolutions that do not neatly fit within the doctrinal rigidities of the selected legal system as an advantage.¹⁸² On the other hand, a non-negligible percentage of users and potential users of the arbitration system may prefer the stricter adherence to legal norms that would be encouraged by a system built on a notion of error correction. For these parties, the process outlined in this Part may provide the conditions for a more rigorous application of the laws they have selected without compromising efficiency of the arbitration procedure too much.

IV. INVESTMENT ARBITRATION AND LAWMAKING

This Part explores whether the introduction of an appellate mechanism in investment arbitration is likely to achieve greater consistency in investment law, as imagined by advocates for the creation of an appeals facility. Based on an examination of pertinent aspects of the operation of the lawmaking function in the United States and in other court systems, it

181. See Carter, *supra* note 133, at 84 (noting that “in international matters in particular, there often is a fear of the unknown and a corresponding tendency for each party to seek as much predictability as possible in the constituting of the tribunal. If each party has the right to select one of the three arbitrators, and some role in the selection of the third, this builds party confidence in the integrity of the process.”).

182. This notion is reflected in the instruction given to courts in England when evaluating arbitral awards for error of law: “The approach is to read an arbitration award in a reasonable and commercial way, expecting, as is usually the case, that there will be no substantial fault that can be found with it.” *AB Attorney General v. Hochtief Airport GmbH*, [2006] 1 A.C. 221 (H.L.). Similarly, Hans Smit has argued that in intra-arbitral review, a deferential “clearly erroneous findings of fact or law” standard is most appropriate, as “[t]he essential nature of arbitration as an efficient and flexible substitute for litigation would be put in jeopardy if provisions were made for plenary review on the facts and the law.” Smit, *supra* note 147, at 1005–06. The error correction process proposed in this Article, in contrast, will not suit parties who wish to grant an arbitrator wide leeway but still want to have the option of appeal in case of an egregious award.

appears doubtful that appellate review would be the best way to achieve the envisioned lawmaking goals.¹⁸³

A. *The Investment Arbitration Framework*

Investment treaties set out to promote foreign investment by granting substantive rights that create a more stable investment climate for citizens of the investor country who invest in the host country.¹⁸⁴ Usually, the sovereign parties commit to provide adequate compensation in case of expropriation, to accord “fair and equitable treatment” and “full protection and security” to investments, and to honor obligations entered into with regard to investments (this last protection is generally re-

183. Not surprisingly, several commentators have spoken out against the introduction of appellate review in investment arbitration. Some have principled objections based on the nature of investment treaties or the arbitration process. See, e.g., Barton Legum, *Visualizing an Appellate System*, in CURRENT ISSUES, *supra* note 3, at 121 (noting that so long as investment treaties retain a bilateral character, an appeals mechanism will do little to resolve inconsistency and is potentially harmful); Jan Paulsson, *Avoiding Unintended Consequences*, in APPEALS MECHANISM, *supra* note 22, at 241, 258–62 (2008) (warning that the appointment of members of an appeals facility would likely re-politicize and de-legitimize a process grounded in party consent); Asif H. Qureshi & Shandana Gulzar Khan, *Implications of an Appellate Body for Investment Disputes from a Developing Country Point of View*, in APPEALS MECHANISM, *supra* note 22, at 267, 277–78 (2008) (noting that the consistency goal may clash with the development interests of developing nations and that, under the current bilateral system, a comprehensive appeals facility is not desirable); cf. Ian Laird & Rebecca Askew, *Finality Versus Consistency: Does Investor-State Arbitration Need an Appellate System?*, 7 J. APP. PRAC. & PROCESS 285, 290 (2005) (presenting the issue as one of balancing “consistency and correctness” with “finality”). Others believe that the practical and logistical hurdles form too great an impediment. See, e.g., Andreas Bucher, *Is There a Need to Establish a Permanent Reviewing Body?*, in THE REVIEW OF INTERNATIONAL ARBITRATION AWARDS 285, 290–92 (Emmanuel Gaillard, ed., 2008) (concluding, because of problems associated with an amendment of the ICSID Convention or with the creation of an optional appeals process, that it is more fruitful to explore other avenues for increasing consistency). A third group maintains that it is too early to assess whether there is a need for an appeals procedure. See, e.g., Laird & Askew, *supra*, at 302.

184. Empirical studies have cast doubt on the assumption that investment treaties result in larger flows of foreign investment. M. Sornarajah, *A Coming Crisis: Expansionary Trends in Investment Treaty Arbitration*, in APPEALS MECHANISM, *supra* note 22, at 39, 39 n.1.

ferred to as an “umbrella clause”).¹⁸⁵ Although the vast majority of investment treaties are bilateral, a few multilateral arrangements exist, for example, the North American Free Trade Agreement (NAFTA).¹⁸⁶

In investment treaties, the sovereigns also consent to arbitrate or litigate disputes regarding substantive treaty provisions. The treaties usually give investor claimants a choice between litigation in the host country and arbitration before tribunals organized under ICSID, the ICC, the Stockholm Chamber of Commerce, or the United Nations Commission on International Trade Law (UNCITRAL).¹⁸⁷ The majority of known investment arbitrations are administered by ICSID.¹⁸⁸ This institution, which specializes in investor-state arbitrations, was established by the Convention on the Settlement of Invest-

185. See, e.g., DUGAN ET AL., *supra* note 5, at 2 (describing the protections to which investors are typically entitled under bilateral and multilateral investment treaties).

186. There is no comprehensive substantive multilateral investment convention to which sovereigns can accede. Attempts by the Organisation for Economic Co-operation and Development to negotiate a Multilateral Agreement on Investment have failed, as have attempts by the WTO to start multilateral negotiations on investment rules. Rainer Geiger, *The Multifaceted Nature of International Investment Law*, in APPEALS MECHANISM, *supra* note 22, at 17, 18.

187. Franck, *supra* note 3, at 1541. As of the end of 2006, ICSID administered almost two-thirds of all known disputes. Approximately twenty-five percent of all known investor-state arbitrations were conducted under the UNCITRAL Rules. Sauvart, *supra* note 22, at 13; see also Andrew P. Tuck, *Investor-State Arbitration Revised: A Critical Analysis of the Revisions and Proposed Reforms to the ICSID and UNCITRAL Arbitration Rules*, 13 LAW & BUS. REV. AM. 885, 886 (2007) (noting that more than half of the BITs provide for ICSID arbitration, and that the UNCITRAL Rules were used in approximately thirty percent of all known investor-state arbitrations).

188. Investment disputes arbitrated outside of ICSID often do not result in publicly available awards. Cf. Ernst-Ulrich Petersmann, *Judging Judges: From “Principal-Agent Theory” to “Constitutional Justice” in Multilevel “Judicial Governance” of Economic Cooperation Among Citizens*, 11 J. INT’L ECON. L. 827, 874 (2008) (“Even though foreign investments often affect public interests, investor-state arbitrations are often submitted to commercial and confidential arbitration procedures . . .”). These disputes only become “known” if enforcement actions in courts ensue or if the parties otherwise make the existence of the arbitration public. Cf. Ernst-Ulrich Petersmann, *International Rule of Law and Constitutional Justice in International Investment Law and Arbitration*, 16 IND. J. GLOBAL LEGAL STUD. 513, 527 (2009) (observing that “commercial arbitration awards remain confidential absent express consent or challenges in national courts . . .”).

ment Disputes between States and Nationals of Other States (the ICSID Convention) of 1965.¹⁸⁹ Proposals for appellate review in investment arbitration have focused on the creation of an appeals facility within the ICSID framework.

Unlike arbitral awards that are governed by the New York Convention, ICSID awards cannot be challenged outside the ICSID framework, effectively precluding review of awards in the national courts in host states.¹⁹⁰ Instead, ICSID has an annulment mechanism under which parties can seek review of awards by an *ad hoc* annulment committee.¹⁹¹ Annulment committees are appointed by the Secretary General and consist of three members who have not served on the first instance tribunal.¹⁹² Annulment is a limited remedy that differs in significant respects from appeal. An annulment committee has only two options: to annul an award in whole or in part, or to let it stand.¹⁹³ It cannot substitute its own opinion for the award, nor can it remand the case to the tribunal that issued the award. Rather, if an award is annulled, either party can request submission of the dispute to a newly appointed tribunal.¹⁹⁴ In addition, the grounds for annulment are limited to (1) improper constitution of the tribunal; (2) manifest excess of the tribunal's powers; (3) corruption on the part of a member of the tribunal; (4) serious departure from a fundamental procedural rule; and (5) failure to state the reasons in the award.¹⁹⁵ As David Caron has explained, the annulment process is limited to a review of the legitimacy of the process, but

189. ICSID Secretariat, *Possible Improvement of the Framework for ICSID Arbitration 1* (Discussion Paper, Oct. 22, 2004), available at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDPublicationsRH&actionVal=ViewAnnouncePDF&AnnouncementType=archive&AnnounceNo=14_1.pdf. The ICSID Convention came into force one year later and currently has 157 signatory states, of which 146 have ratified or accepted the Convention. A list of signatories, ratifications and acceptances is available at <http://icsid.worldbank.org>.

190. ICSID Convention, *supra* note 25, art. 53, ¶1 ("The award shall be binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in this Convention.")

191. Non-ICSID investment arbitration awards are subject to challenges under the New York Convention framework. See Tams, *supra* note 35, at 11.

192. ICSID Convention, *supra* note 25, art. 52, ¶3.

193. *Id.*

194. *Id.* ¶6.

195. *Id.* ¶1(a)-(e).

it does not extend to the substantive correctness of the award under review.¹⁹⁶

B. *The Search for a Solution to Incoherence*

The question of whether international investment law will develop into a coherent legal system is acute, in part, because of the field's astonishing growth in recent years. The number of bilateral investment treaties (usually referred to as BITs) has grown from less than four hundred in the late 1980s to approximately three thousand today.¹⁹⁷ Investor-state arbitrations are on the rise as well. For about thirty years after the ICSID Convention entered into force, ICSID registered less than a handful of cases per year. In fact, it was not unusual for a year to go by without the registration of any new ICSID cases. Starting in 1997, however, the number of new cases has consistently been in the double digits, and in 2011 alone, thirty-eight new cases were registered with ICSID.¹⁹⁸ The proliferation of bilateral treaties and the tremendous increase in case load have contributed to fragmentation, a trend that will likely continue. In light of these characteristics of investment law, the question is whether the creation of an appeals facility within the ICSID framework is likely to achieve the increased coherence its proponents seek to achieve.¹⁹⁹

196. Caron, *supra* note 78, at 24 (“[A]ppeal generally focuses upon both the legitimacy of the process of decision and the substantive correctness of the decision. *Annulment*, on the other hand, and particularly in the case of arbitration, focuses not on the correctness of the decision, but rather more narrowly considers whether, regardless of errors in application of law or determination of fact, the decision resulted from a legitimate process.”).

197. As of the end of 2010, 2,807 BITs had been concluded. UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT (UNCTAD), WORLD INVESTMENT REPORT 2011 100, available at <http://www.unctad-docs.org/files/UNCTAD-WIR2011-Full-en.pdf>.

198. ICSID, THE ICSID CASELOAD—STATISTICS 7, 20 (2012), available at <http://icsid.worldbank.org>.

199. Asif Qureshi and Shandana Khan point out that investment arbitration “is largely set against a *normative* framework that is bilateral, disorganized and non-multi-lateral” and ask, rhetorically, “Is it really possible to meaningfully evaluate the arguments for and the obstacles in setting up an appellate facility in the investment sphere, with the objective of providing normative coherence, in circumstances in which the multilateral consensus on substantive matters is not very evident?” Qureshi & Khan, *supra* note 183, at 272.

1. *The Argentina Cases*

Considering the decentralized nature of arbitration, awards from investment arbitrators show remarkable consistency. For example, based on an examination of investment awards, Gabrielle Kaufmann-Kohler has concluded that case law addressing the distinction between treaty and contract claims and the fair and equitable treatment standard is consistent.²⁰⁰ Yet inconsistency exists in certain controversial areas, such as the application of the necessity defense.²⁰¹ The awards and annulment decisions that have so far been issued in the more than forty cases filed against Argentina with ICSID in the past ten years leave no doubt that the risk of inconsistent outcomes and reasoning is a real one. A brief discussion of five of these cases, all of which were brought under the United States-Argentina BIT, illustrates the form disagreement among investment tribunals can take.

The claimants in these cases had invested in Argentine companies as part of Argentina's privatization program in the early 1990s. In four cases, brought by CMS Gas Transmission Co., LG&E Energy Corp., Enron Creditors Recovery Corp., and Sempra Energy International, the investments were in the gas sector.²⁰² In the fifth one, brought by Continental Casualty Co., the investment was in the insurance industry.²⁰³ In these investment transactions, Argentina had made commitments aimed at stabilizing the tariff structure notwithstanding the strong fluctuation of the peso. Specifically, Argentina un-

200. Gabrielle Kaufmann-Kohler, *Is Consistency a Myth?*, in PRECEDENT IN INTERNATIONAL ARBITRATION (Yas Banifatemi ed., 2007), at 137, 138–41.

201. *Cf. id.* at 142–43.

202. CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/8, Award (May 12, 2005) [hereinafter CMS Award]; CMS Gas Transmission Co. v. Argentine Republic, ICSID Case No. ARB/01/8, Annulment Decision (Sept. 25, 2007) [hereinafter CMS Annulment Decision]; Enron Award, *supra* note 32; Enron Annulment Decision, *supra* note 32; LG&E Energy Corp. v. Argentine Republic, ICSID Case No. ARB/02/1, Decision on Liability (Oct. 3, 2006) [hereinafter LG&E Decision on Liability]; Sempra Energy Int'l v. Argentine Republic, ICSID Case No. ARB/02/16, Award (Sept. 28, 2007) [hereinafter Sempra Award]; Sempra Energy Int'l v. Argentine Republic, ICSID Case No. ARB/02/16, Annulment Decision (June 29, 2010) [hereinafter Sempra Annulment Decision].

203. Cont'l Cas. Co. v. Argentine Republic, ICSID Case No. ARB/03/9 (Sept. 5, 2008) [hereinafter Continental Award], Annulment Decision (Sept. 16, 2011) [hereinafter Continental Annulment Decision].

dertook to calculate tariffs collected by Argentine subsidiaries in U.S. dollars converted into pesos. Argentina also consented to adjust the tariffs twice a year.²⁰⁴ Approximately ten years later, Argentina suffered an unprecedented economic meltdown. The Argentine government took a series of measures to address the crisis, including the enactment of an Emergency Law in January 2002, which abrogated the tariff conversions and semi-annual tariff adjustments.²⁰⁵ The investors who filed claims with ICSID claimed that Argentina's actions violated several obligations under the BIT, including the obligations to accord fair and equitable treatment to investments and to honor commitments made to investors.²⁰⁶ Argentina argued, among other things, that it was not liable as a result of the necessity defense under customary international law and the BIT's emergency clauses, chiefly Article XI.²⁰⁷

The inconsistency is immediately apparent from the outcomes in the five cases. In *CMS*, *Enron* and *Sempra*, the tribunals held that Argentina did not meet the standards for the defenses.²⁰⁸ In *LG&E* and *Continental*, the tribunals held that Argentina had established the defense, but they applied it differently, resulting in inconsistent rulings regarding the extent of Argentina's liability.²⁰⁹ The conflicting outcomes reflect differences in factual assessments, as well as disagreement about the relationship between the defenses under, respectively, the treaty and customary international law.²¹⁰ Article XI

204. See, e.g., CMS Award, *supra* note 202, ¶¶ 53–57 (describing CMS's understanding of such a commitment by Argentina).

205. E.g., *id.* ¶ 65.

206. E.g., *id.* ¶ 88.

207. See, e.g., *id.* ¶¶ 91–99.

208. *Id.* ¶ 331; Enron Award ¶¶ 313, 321, 339; Sempra Award ¶ 388.

209. LG&E Decision on Liability ¶¶ 257–63; Continental Award ¶¶ 219–22, 266.

210. Notably, there is substantial overlap in arbitrators in the Argentina cases. Francisco Orrego-Vicuña was the chair in the *CMS*, *Enron* and *Sempra* tribunals. CMS Award, *supra* note 202, ¶ 11; Enron Award, *supra* note 32, ¶ 12; Sempra Award, *supra* note 202, ¶ 10. Marc Lalonde sat on the *CMS* and *Sempra* tribunals, and was appointed by the claimants in both cases. CMS Award, *supra*, ¶ 10; Sempra Award, *supra*, ¶ 10. Two arbitrators served in tribunals that issued inconsistent awards. Francisco Rezek was a member of the *CMS* and *LG&E* tribunals, and was in both cases appointed by Argentina. CMS Award, *supra*, ¶ 10; LG&E Decision on Liability, *supra* note 202, ¶ 6. Albert Jan van den Berg was a member of the *LG&E* and *Enron* tribunals. In the *LG&E* case, he was appointed by the claimant. LG&E Decision on Lia-

of the BIT reserves the right of the sovereigns to take “measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests.”²¹¹ The treaty text thus provides little guidance as to the content of necessity. In contrast, Article 25 of the International Law Commission’s Articles on State Responsibility, which codifies the emergency defense, lists specific elements.

The approaches taken by the tribunals and annulment committees could be grouped in three categories.²¹² The first approach, taken by the tribunals in *CMS*, *Enron*, and *Sempra*, is that the necessity defense under customary international law supplies the standards for assessing whether the BIT defense has been met. The *CMS*, *Enron*, and *Sempra* awards essentially follow the same script. The tribunals first analyze Argentina’s defense under customary international law as codified by the International Law Committee in the Articles on State Responsibility.²¹³ Turning to Article XI, the tribunals then state that the defense must be interpreted by reference to the elements of a state of emergency under customary international law.²¹⁴

bility, *supra*, ¶ 6. In the *Enron* case, he was appointed by the chair, when the arbitrator initially appointed by Argentina resigned almost five years into the arbitration proceedings. *Enron Award*, *supra*, ¶¶ 11, 39. Cf. David Schneiderman, *Judicial Politics and International Investment Arbitration: Seeking an Explanation for Conflicting Outcomes*, 30 NW. J. INT’L L. & BUS. 383 (2010) (exploring potential explanations for the outcome in *LG&E* even though two of the three arbitrators sat on tribunals that rendered conflicting awards). As for annulment committee appointments, Gavan Griffith sat on the *Enron* and *Continental* committees, and Christer Söderlund sat on the *Sempra* and *Continental* committees. *Enron Annulment Decision*, *supra* note 202, ¶ 7; *Continental Annulment Decision*, *supra* note 203, ¶ 4; *Sempra Annulment Decision*, *supra* note 202, ¶¶ 5, 7.

211. Treaty Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Arg., art. XI, Nov. 14, 1991, S. Treaty Doc. No. 103-2.

212. This part of the discussion draws on an illuminating presentation by Michael Nolan, titled *The Dynamic Relationship Between the Customary International Law of Investment Protection and Bilateral Investment Treaties* (Columbia Law School International Investment Law and Policy Speaker Series, March 19, 2012).

213. *CMS Award*, *supra* note 202, ¶¶ 315–31; *Enron Award*, *supra* note 32, ¶¶ 303–13; *Sempra Award*, *supra* note 202, ¶¶ 344–55.

214. *CMS Award*, *supra* note 202, ¶ 374; *Enron Award*, *supra* note 32, ¶ 334; *Sempra Award*, *supra* note 202, ¶ 378.

The *Enron* and *Sempra* tribunals explicitly justified this approach against the argument, submitted in an expert opinion, that a treaty is distinct from, and takes priority over, customary international law. The *Enron* tribunal, while acknowledging that “a treaty regime specifically dealing with a given matter will prevail over more general rules of customary international law[,]” observed that this was not the situation presented by the U.S.-Argentina BIT.²¹⁵ The tribunal noted that because the BIT does not specify the elements of necessity, the BIT defense “becomes inseparable from the customary law standard insofar as the conditions for the operation of state of necessity are concerned.”²¹⁶

The second approach, taken by the *LG&E* tribunal and the *CMS* annulment committee, is that the two defenses are distinct and stand in a hierarchical relationship to one another. The *CMS* annulment committee provides the most elaborate explanation of this position. Its decision explains that Article XI concerns wrongfulness, meaning that acts covered by it cannot be held to be in breach of the BIT obligations. With regards to Article 25, it is unclear whether it addresses wrongfulness or liability.²¹⁷ If Article 25 also addresses wrongfulness, Article XI would be the *lex specialis* as to that issue and apply at the exclusion of customary law.²¹⁸ If Article 25 goes to liability, it would still be a secondary rule that the tribunal should consider only after determining that Article XI did not preclude a finding of breach.²¹⁹ The *LG&E* tribunal had already applied some aspects of this approach before the *CMS* committee issued its annulment decision. Specifically, the *LG&E* tribunal concluded that the measures taken by the Argentine government fell within the Article XI defense²²⁰

215. *Enron Award*, *supra* note 32, ¶ 334.

216. *Id.*; see also *Sempra Award*, *supra* note 202, ¶ 378. The *CMS* tribunal, which was the first to issue an award, had followed this approach without expressly justifying it. See *CMS Award*, *supra* note 202, ¶ 374 (noting that the tribunal’s review of Argentina’s defense under the BIT involved “a substantive review that must examine whether the state of necessity or emergency meets the conditions laid down by customary international law and the treaty provisions and whether it thus is or is not able to preclude wrongfulness.”).

217. *CMS Annulment Decision*, *supra* note 202, ¶¶ 129, 132.

218. *Id.* ¶ 133.

219. *Id.* ¶ 134.

220. *LG&E Decision on Liability*, *supra* note 202, ¶¶ 226–42.

and noted that this effectively ended the inquiry.²²¹ Although the tribunal proceeded to address the necessity defense under customary international law, it characterized this analysis as one that provided further “support” for its conclusions regarding Argentina’s defense under the BIT.²²²

The third approach was introduced by the *Continental* tribunal. Like the *LG&E* tribunal and the *CMS* annulment committee, the *Continental* tribunal rejected the position, taken by the other three tribunals, that the treaty and customary law defenses are “inseparable.”²²³ Yet where the *LG&E* tribunal engaged purely in textual analysis to determine whether the evidence established the defense, the *Continental* tribunal looked for guidance on the concept of necessity outside the investment treaty context. The tribunal noted that Article XI could be traced back to the Friendship, Commerce, and Navigation treaties entered into by the United States and, eventually, to a specific provision in the General Agreement on Tariffs and Trade (GATT) of 1947.²²⁴ The tribunal therefore decided that it is “appropriate to refer to the GATT and WTO case law which has extensively dealt with the concept and requirements of necessity in the context of economic measures derogating to the obligations contained in GATT[.]”²²⁵

Although the *LG&E* and the *Continental* tribunals both honored Argentina’s necessity defense under the BIT, the awards differ in their analysis of the consequences of the applicability of Article XI. The analysis of the *LG&E* tribunal on this point, moreover, also appears to be inconsistent with the reasoning of the *CMS* annulment committee. Specifically, in analyzing the treaty defense the *LG&E* tribunal does not appear to distinguish between wrongfulness and liability. In fact, it uses both terms in connection with the treaty defense, stating in a single sentence that “Article XI establishes the state of necessity as a ground for exclusion from *wrongfulness* of an act of the State, and therefore, the State is exempted from *liability*.”²²⁶ The *LG&E* tribunal, which had earlier held that Argen-

221. *Id.* ¶ 245.

222. *Id.*

223. Continental Award, *supra* note 203, ¶ 192.

224. *Id.*

225. *Id.*

226. LG&E Award, *supra* note 202, ¶ 261 (emphasis added).

tina had breached its fair and equitable treatment obligations under the umbrella clause,²²⁷ further interpreted Article XI as providing protection only during the state of necessity.²²⁸ Consequently, it held that Argentina's obligations under the BIT reemerged once the state of necessity had passed, and that Argentina started incurring liability on that date.²²⁹ The *Continental* tribunal, on the other hand, held that due to the protections accorded by Article XI, the measures taken by Argentina during the economic collapse were not in breach of the BIT obligations.²³⁰ As a result, the claimants were entitled only to damages that resulted from measures taken after the crisis was over.²³¹

The annulment decisions in *CMS*, *Enron*, and *Sempra* all offer harsh criticisms of the awards they were reviewing. Yet this is where the unity ends. Not only do the decisions continue to reflect different substantive approaches, they also reveal disagreement about the proper application of the "manifest excess of powers" ground for annulment. The *CMS* committee, as noted, identified two errors in the *CMS* award: the conflation of the two defenses, and the failure to give priority to the treaty defense. The committee noted that the award constituted "a manifest error of law" that may well have determined the outcome.²³² Yet it let the award stand, aside from a technical partial annulment of a different section of the award that did not affect the validity of the award as a whole.²³³ In so

227. *Id.* ¶¶ 132, 175.

228. *Id.* ¶ 261.

229. *Id.*

230. *Continental Award*, *supra* note 202, ¶ 164.

231. *Id.* ¶¶ 220–22.

232. *CMS Annulment Decision*, *supra* note 202, ¶¶ 129–30, 135.

233. *Id.* ¶ 163. Although this rendered the *CMS* award final, Argentina has to date refused to make any payments toward the \$133.2 million it was ordered to pay. Argentina reportedly took the position that CMS had to seek enforcement in the Argentine courts, which CMS refused. Luke E. Peterson, *Argentine Crisis Arbitration Awards Pile Up, but Investors Still Wait for a Payout*, Law.com (June 25, 2009), available at <http://justinvestment.org/2009/07/argentine-crisis-arbitration-awards-pile-up-but-investors-still-wait-for-a-payout>. CMS eventually transferred the award to Blue Ridge Investments, a subsidiary of Bank of America. Argentina's failure to pay the CMS award and a second final ICSID award in favor of another American investor, Azurix Corp., has now resulted in political sanctions: On March 26, 2012, President Barack Obama announced a suspension of Argentina's trade benefits under the U.S. Generalized System of Preferences program due to its

doing, the CMS committee noted that wrong application of the law does not constitute manifest excess of powers and that it “cannot simply substitute its own view of the law and its own appreciation of the facts for those of the Tribunal.”²³⁴

In contrast, the *Enron* and *Sempra* committees annulled the awards based on excess of powers due to the failure of the tribunal to apply the applicable law. The analysis followed by each tribunal, however, was different. The *Sempra* committee ruled that the tribunal had failed to apply the pertinent BIT provisions because it had used customary international law as the primary source of law.²³⁵ The *Enron* annulment committee, on the other hand, based the annulment on its conclusion that the tribunal had failed to apply customary international law.²³⁶

The annulment committees’ divergent views regarding the excess of powers ground may well turn out to be a greater challenge to international investment law than the substantive disagreements among tribunals. After all, the interpretation of the annulment grounds directly implicates a control mechanism that is intended to guard the legitimacy of the arbitration framework itself.²³⁷ The Argentina annulment decisions have rekindled the flames of a long-standing debate about the

failure to pay the awards. Doug Palmer, *Obama Says to Suspend Trade Benefits for Argentina*, Reuters.com (Mar. 26, 2012), available at <http://www.reuters.com/article/2012/03/26/us-usa-argentina-trade-idUSBRE82P0QX20120326>.

234. *Id.* ¶ 136.

235. *Sempra* Annulment Decision, *supra* note 202, ¶¶ 196–219.

236. *Enron* Annulment Decision, *supra* note 32, ¶¶ 386–95. The *Continental* and *LG&E* cases also proceeded to annulment. The *Continental* annulment committee let the award stand. *Continental* Annulment Decision, *supra* note 202. In *LG&E*, the parties have suspended the proceedings, presumably because they are trying to work out a settlement. See the case information, available at <http://icsid.worldbank.org/ICSID/FrontServlet> (last visited Apr. 29, 2012). In *Enron* and *Sempra*, new tribunals have been appointed. *Id.*

237. In an article that offers insights on the institution of annulment and the challenges it faces that are still astute, Michael Reisman describes the distinction between control and appeal as follows: “Appeal is concerned with what is right for the parties and is initiated by the parties. Control is concerned with maintenance of the minimum conditions necessary for the continuation of the process of decision itself.” W. Michael Reisman, *The Breakdown of the Control Mechanism in ICSID Arbitration*, 1989 DUKE L.J. 739, 748.

scope of permissible review by annulment committees.²³⁸ Indeed, the ICSID Secretariat announced recently that it will prepare a paper on the annulment process. This step was taken after the Philippines raised concerns about the process at an Administrative Council meeting and proposed the creation of a task force to examine potential improvements.²³⁹

2. *The Envisioned Role of an Appeals Facility*

The principal argument for the creation of an ICSID appeals facility is the expectation that it would promote coherence in investment law and, as a consequence, increase predictability.²⁴⁰

Proponents of appellate review argue that the unpredictability resulting from inconsistent awards, like those rendered in the cases against Argentina, undermines the legitimacy of

238. See, e.g., Dohyun Kim, *The Annulment Committee's Role in Multiplying Inconsistency in ICSID Arbitration: The Need to Move Away from an Annulment-Based System*, 86 N.Y.U. L. REV. 242, 250–52 (2011) (arguing that in a recent series of decisions, annulment committees seem to be engaging in greater substantive review of tribunals' awards, suggesting confusion among annulment committees of their role in the ICSID arbitration system); Bart M.J. Szewczyk, *Sempre Energy International v. Argentine Republic*, 105 AM. J. INT'L L. 547, 551 (2011) (criticizing the *Sempre* annulment decision for blurring the line between misapplication of the law and failure to apply the law).

239. Luke Eric Peterson, *ICSID to Prepare "Background Paper" on Annulment Process, Following Request by Philippines; German Investor Criticizes Effort by Philippines*, iareporter.com (Oct. 5, 2011), available at http://www.iareporter.com/articles/20111005_1.

240. See Franck, *supra* note 3, at 1617–18 (“A single, unified, permanent body . . . will enhance the probability of centralization and standardization”); Kim, *supra* note 238, at 276 (arguing that there is a “need for an appeals mechanism to instill a norm of coherence in ICSID decisions.”); Howard Mann, *Transparency and Consistency in International Investment Law: Can the Problems be Fixed by Tinkering?*, in *APPEALS MECHANISM*, *supra* note 22, at 213, 220 (“Introducing an appellate level would . . . have the impact of imposing consistency, and thus greater clarity, for both host countries and investors.”); VAN HARTEN, *supra* note 25, at 164 (noting the concern that investment arbitration lacks coherence and stating that “[t]he difficulty in investment treaty arbitration arises from the system’s fragmented and individualized structure . . . and, specifically, from the absence of an appellate institution”); cf. Katia Yannaca-Small, *Improving the System of Investor-State Dispute Settlement: The OECD Governments’ Perspective*, in *APPEALS MECHANISM*, *supra* note 22, at 223, 224, 226 (the OECD considered avoidance of inconsistent awards a main advantage of an appeals procedure, but the majority of OECD governments believed a “radical system change” was not warranted).

investment law. Susan Franck, a vocal advocate for the promotion of coherence in investment arbitration, has put it as follows:

Legitimacy depends in large part upon factors such as determinacy and coherence, which can in turn beget predictability and reliability. Related concepts such as justice, fairness, accountability, representation, correct use of procedure, and opportunities for review also impact conceptions of legitimacy. When these factors are absent individuals, companies and governments cannot anticipate how to comply with the law and plan their conduct accordingly, thereby undermining legitimacy.²⁴¹

In addition to enhancing predictability, consistency also ensures that like cases are treated the same. Some have argued that a dispute settlement system that violates this fundamental principle of fairness is ultimately unsustainable.²⁴² A few commentators go so far as to claim that the lack of coherence has resulted in a legitimacy crisis in investment arbitration, which in turn will have negative consequences for international investments.²⁴³ Several authors identify the absence

241. Franck, *supra* note 3, at 1584 (footnotes omitted); see also Charles H. Brower, II, *Structure, Legitimacy, and NAFTA's Investment Chapter*, 36 VAND. J. TRANSNAT'L L. 37, 51 (2003) ("[I]nternational legal regimes depend for their survival on perceptions of legitimacy To generate perceptions of legitimacy, legal regimes must operate predictably, conform to historical practice, and incorporate fundamental values shared by the governed community.") (footnotes omitted); Bucher, *supra* note 183, at 285 (noting that the lack of consistency in investment arbitration awards creates "uncertainty" and "has a negative impact on the authority that the ICSID system should command."); THOMAS M. FRANCK, *THE POWER OF LEGITIMACY AMONG NATIONS* 52 (1990) (identifying "determinacy" and "coherence" as two of four indicators of rule legitimacy); Johanna Kalb, *Creating an ICSID Appellate Body*, 10 UCLA J. INT'L L. & FOREIGN AFF. 179, 196–200 (2005) (arguing that inconsistent arbitration awards undermine international investment).

242. Michael D. Goldhaber, *Wanted: A World Investment Court*, *The American Lawyer*, Summer 2004, reprinted in 1 TRANSNAT'L DISPUTE MGMT., JUL. 2004, at 1, 1 (quoting Nigel Blackaby, a prominent investment arbitration practitioner, as saying that a system in which inconsistent awards are rendered "cannot last long. It shocks the sense of rule of law or fairness."); see also Franck, *supra* note 3, at 1583; Franck, *supra* note 25, at 65–66.

243. Sornarajah, *supra* note 184, at 41–42 (arguing that a legitimacy crisis has arisen as a result of the exploding number of arbitrations, coupled with the absence of a control mechanism and the fact that most arbitrators come

of appellate review as a factor contributing to the lack of consistency.²⁴⁴ The existing framework, however, is not equipped to engender greater coherence. The goal cannot be achieved through the annulment process. This is not only a function of the limited nature of annulment review due to the constraints imposed by the grounds for annulment, but also a natural result of the *ad hoc* character of annulment review. There is no reason why a committee whose mandate is limited to the review of a single case will have a greater claim to authority than the tribunal whose award it reviews. Those who seek to increase coherence have therefore proposed several reforms, including the establishment of a permanent appeals facility.²⁴⁵

The idea of implementing appellate review in investment arbitration gained momentum in 2004, when the ICSID Secretariat published a discussion paper in which it raised the ques-

from commercial arbitration backgrounds and may not be as sensitive to the public nature of the interests involved); *see also* Brower, *supra* note 241, at 93 (concluding that the investment chapter of NAFTA “finds itself in the midst of a legitimacy crisis,” in part as a result of incoherent decisions from *ad hoc* tribunals); Franck, *supra* note 3, at 1586. *But see* Devashish Krishan, *Thinking About BITs and BIT Arbitration: The Legitimacy Crisis That Never Was*, in *NEW DIRECTIONS IN INTERNATIONAL ECONOMIC LAW: IN MEMORIAM THOMAS WÄLDE* (Todd Weiler & Freya Baetens eds., 2011) at 107, 110–16 (arguing that the term “legitimacy crisis” distorts the discussion as there is no legitimacy crisis in investment arbitration and none is looming); Paulsson, *supra* note 183, at 241 (“What issues of coherence? . . . From a practitioner’s viewpoint, there is no crisis of unpredictability.”).

244. Burke-White & von Staden, *supra* note 27, at 299 (“These contradictory awards and the lack of a coherent or consistent standard of review are especially problematic given that the ICSID Convention lacks meaningful appellate review . . .”); *see also* Blackaby, *supra* note 27, at 364 (“An appeal on specific points of law would avoid the risk of an aberrant decision and be more likely to result in coherent jurisprudence.”).

245. Franck, *supra* note 3, at 1617–25; Gantz, *supra* note 3, at 73; Gleason, *supra* note 75, at 285–86; *cf.* Brower, *supra* note 241, at 91–94 (arguing for the creation of a standing appellate body in the NAFTA framework). Gus Van Harten has described a detailed proposal for a free-standing “international investment court” modeled after the International Court of Justice. VAN HARTEN, *supra* note 25, at 180–84. A permanent appeals facility makes more sense than *ad hoc* appellate solutions, in light of the stated purpose of promoting the development of a coherent body of law. *Cf.* Geiger, *supra* note 186, at 26 (noting that “it is difficult to conceive how the coherence of awards would be increased by an *ad hoc* appeals procedure, in the absence of a permanent international tribunal that has no institutional basis in the current system.”).

tion of whether it should seek to create an appeals facility.²⁴⁶ While taking the position that ICSID awards did not present significant inconsistencies (the publication of this paper predated the conflicting Argentina awards), the Secretariat acknowledged the *potential* for the development of inconsistent standards and suggested that an appeals facility might foster coherence.²⁴⁷ The Secretariat took note of initiatives to develop appeal mechanisms for investor-state arbitrations outside the ICSID framework²⁴⁸ and observed that a single, permanent appeals facility within ICSID would be preferable.²⁴⁹ Yet the paper identified drawbacks as well, including the reduced finality of awards and the potential for delays in enforcement.²⁵⁰ An annex to the discussion paper outlined some possible features of a proposed appeals facility. ICSID suggested that an appeals facility consist of fifteen arbitrators, which would sit in panels of three.²⁵¹ Appellate panels would review awards for clear error of law or any of the five grounds for annulment under the ICSID Convention and possibly for “serious errors of fact.”²⁵²

246. ICSID Secretariat, *supra* note 189, at 14–16.

247. *Id.* at 14–15.

248. Prior to the ICSID discussion paper, the United States had endorsed the creation of an appeals process in investment arbitrations in the Trade Act of 2002, which provided: “[T]he principal negotiating objectives of the United States regarding foreign investment are . . . to secure for investors important rights comparable to those that would be available under United States legal principles and practice, by . . . providing for an appellate body or similar mechanism to provide coherence to the interpretations of investment provisions in trade agreements” Bipartisan Trade Promotion Authority Act, 19 U.S.C. § 3802(b)(3)(G)(iv) (2006). BITs concluded after the Trade Protection Act was enacted (including with Chile, Uruguay, and Singapore), and the U.S. Model BIT as revised in 2004, include provisions under which the parties agree to consider the establishment of an appeals mechanism in the future. *See, e.g.*, Free Trade Agreement, U.S.-Chile, Annex 10-H, June 6, 2003, available at <http://www.ustr.gov/trade-agreements/free-trade-agreements/chile-fta>; U.S. Model Investment Bilateral Treaty, Annex D, Nov. 2004, available at <http://www.state.gov/e/eeb/ifd/bit>; *see also* Tams, *supra* note 35, at 5 (“Recent US [sic] investment treaties . . . as well as the 2004 U.S. Model B.I.T. envisage the establishment of an investment appeals tribunal . . .”).

249. ICSID Secretariat, *supra* note 189, at 15–16.

250. *Id.* at 15. Of course, finality is already somewhat compromised as a result of the availability of an annulment procedure.

251. *Id.*, Annex at 3.

252. *Id.*, Annex at 4.

A year later, the ICSID Secretariat announced that it would not pursue an appeals facility at that time, noting that most commentators had indicated that the creation of an appeals mechanism was “premature” in light of technical and policy issues identified in the earlier paper.²⁵³ The Secretariat stated that it would “continue to study” these issues.²⁵⁴

C. *Appellate Review and Lawmaking*

1. *Lawmaking by Adjudicators*

Lawmaking refers, broadly, to the creation and refinement of substantive law by adjudicators. Because of law’s indeterminate nature, judges and other decision-makers play a critical role in shaping legal rules and standards through interpretation and application.²⁵⁵ The scope and extent of lawmaking by adjudicators is not constant; there is considerable variation among legal systems and between different fields within a legal system. Even within a single field in a particular jurisdiction, the amount of discretion exercised by adjudicators will differ from time to time, depending on such things as the amount of space applicable statutes leave for interpretation and the prevailing attitudes regarding adjudicative lawmaking. In the United States, courts have traditionally played a prominent role as lawmakers in the areas that were the subject of common law. They also play a significant role in the development and harmonization of the application of statutory norms and the interpretation of the United States Constitution and the state constitutions. Many civil law systems, on the other hand, have strongly resisted the notion that adjudicators engage in lawmaking, rather than pure law application. The aversion against adjudicatory lawmaking is based on the theory that the separation of powers requires that lawmaking be exclusively reserved for the legislature.²⁵⁶ But courts in civil law jurisdictions interpret legal texts and apply legal rules to specific facts, which are activities that contribute to the refinement of the

253. ICSID Secretariat, *Suggested Changes to the ICSID Rules and Regulations* 4 (Working Paper May 12, 2005), available at <http://icsid.worldbank.org>.

254. *Id.*

255. ALEC STONE SWEET, *THE JUDICIAL CONSTRUCTION OF EUROPE* 9 (2004).

256. JOHN HENRY MERRYMAN & ROGELIO PÉREZ-PERDOMO, *THE CIVIL LAW TRADITION* 23–24 (3d ed. 2007).

law.²⁵⁷ Moreover, many civil law jurisdictions have moved toward increased judicial power, especially in the constitutional context.²⁵⁸ Investment arbitrators undoubtedly engage in lawmaking in the broadest sense. As adjudicators who have the last word on the interpretation of investment treaties, the relevance of investment awards extends far beyond the disputes they resolve.

Lawmaking in court systems often involves a coordinated endeavor to develop law in a coherent way. Appellate review serves two specific goals in this process: the promotion of uniformity of decisions, and the adaptation of an existing body of substantive law to meet new situations and changing circumstances.²⁵⁹ These goals exist in tension with each other: True uniformity requires strict adherence to earlier decisions, while the second aspect mandates that, when the situation calls for it, earlier decisions be bent or even overruled.²⁶⁰ Adding to these internal pressures are systems of checks and balances that create a certain degree of friction between tenured judges and a democratically-elected legislature. To maintain legitimacy in this environment, appellate courts must walk a tightrope between continuity and change. As a result, lawmaking by domestic courts tends to be incremental.²⁶¹ Incremental-

257. Cf. HANS KELSEN, *PURE THEORY OF LAW* 234 (1934) (arguing no categorical distinction can be made between law-creation and law-application); cf. Armin von Bogdandy, Ingo Venzke, *Beyond Dispute: International Judicial Institutions as Lawmakers*, 12 GERMAN L. REV. 979, 984–89 (2011).

258. MERRYMAN & PÉREZ-PERDOMO, *supra* note 256, at 38; ALEC STONE SWEET, *GOVERNING WITH JUDGES: CONSTITUTIONAL POLITICS IN EUROPE* 116–24 (2000) (discussing development toward increased constitutional review by judges in Germany, Italy, Spain and France); *id.* at 127–29 (describing examples of lawmaking through statutory interpretation by judges in these jurisdictions in areas other than constitutional law).

259. Frisch, *supra* note 1, at 75–76; cf. CARRINGTON, *supra* note 1, at 2–3.

260. See Carrington, *supra* note 118, at 554 (“The lawmaking role requires a delicate balance between the importance of flexibility in the national law and the importance of stability of doctrine.”); Frank H. Easterbrook, *Stability and Reliability in Judicial Decisions*, 73 CORNELL L. REV. 422, 423 (1988) (“Th[e] possibility of improvement makes precedent unstable There is an equilibrium degree of disequilibrium.”); Frederick Schauer, *Precedent*, 39 STAN. L. REV. 571, (1987) (“We attain predictability . . . only by diminishing our ability to adapt to a changing future.”).

261. Cf. MARTIN SHAPIRO & ALEC STONE SWEET, *ON LAW, POLITICS, AND JUDICIALIZATION* 93 (2002) (noting that “the rules or practices of *stare decisis* [are] simply those of incrementalism stated in other terms.”).

ism has also been observed in the case law of the WTO Appellate Body.²⁶² Here again, part of the explanation for the incremental mode of law development may be found in legitimacy concerns, albeit of a different nature from those in national legal systems. Specifically, because the counterbalance of a legislature is lacking, the WTO Appellate Body has more flexibility than many domestic courts but it is also vulnerable to the accusation of unchecked “activism.”²⁶³ Notwithstanding these legitimacy concerns, the WTO Appellate Body has been particularly effective in shaping trade law, a process some observers have referred to as “constitutionalization.”²⁶⁴

Incremental change guided by an ultimate decision-maker is the most orderly way in which lawmaking can proceed. It is not, however, the only way to create law, and the model is not feasible or even desirable in every context. In national legal systems, courts develop law through a dialogue with an identifiable, if shifting, legislature. In trade law, the

262. See Robert Howse, *Moving the WTO Forward—One Case at a Time*, 42 CORNELL INT’L L.J. 223, 223–24 (2009) (arguing that “[t]he WTO dispute settlement system has demonstrated its efficacy by evolving incrementally through practice without a formal change in the treaty mandate that established and defined the parameters of that system”).

263. See, e.g., Michael Ioannidis, *A Procedural Approach to the Legitimacy of International Adjudication: Developing Standards of Participation in WTO Law*, 12 GERMAN L.J. 1175, 1190–91 (2011) (“Taking into consideration the lack of an effective legislating mechanism, the interpretation of international trade rules by the adjudicating bodies may thus be addressed as a fairly ‘cemented’ set of norms, which is little adaptive to the developing interests of those it affects or the differing choices of subsequent domestic parliamentary majorities.”); cf. Bogdandy & Venzke, *supra* note 257, at 994 (“International courts do not operate as parts of polities that include functioning political legislatures. Once an international agreement is in place, it is largely withdrawn from the grasp of its individual makers.”). José Alvarez has observed that investment law presents similar issues. José E. Alvarez, *The Emerging Foreign Direct Investment Regime*, 99 AM. SOC. INT’L L. & PROC. 94, 96 (2005) (“The emerging FDI regime draws some of the same ‘democratic’ critiques as more institutionalized international regimes: namely, that the law that it relies on is not accountable or respectful of traditional notions of separation of powers.”).

264. See, e.g., Sungjoon Cho, *Global Constitutional Lawmaking*, 31 U. PA. J. INT’L L. 621 (2010); Jeffrey L. Dunoff, *Constitutional Conceits: The WTO’s “Constitution” and the Discipline of International Law*, 17 EUR. J. INT’L L. 647, 651–56 (2006); Deborah Z. Cass, *The “Constitutionalization” of International Trade Law: Judicial Norm-Generation as the Engine of Constitutional Development in International Trade*, 12 EUR. J. INT’L L. 39 (2001).

Appellate Body evaluates the application and interpretation of a specified group of international instruments—the “covered agreements” as defined in the Dispute Settlement Understanding. Investment arbitration, in contrast, is a field without a discernible legislature or a discrete body of law. An ICSID appeals facility would be tasked with imposing coherence in the face of an ever-growing number of bilateral treaties negotiated at different times, with differing terms that were drafted in response to evolving standards.²⁶⁵ Moreover, due to the nature of the interests involved, in investment law coherence will always compete with other values, including development, environmental, and human rights interests. The balance between a host state’s interest in retaining flexibility to respond to economic crises and an investor’s interest in stability will be struck differently depending on the text of the treaty and the circumstances under which it was negotiated.²⁶⁶ Some observers have

265. By way of example, investment treaties have become more protective of the states’ interests; as industrialized economies found themselves regularly on the receiving end of investments, investment treaties have become more balanced. Geiger, *supra* note 186, at 19–20; see also Sornarajah, *supra* note 184, at 40 (“The United States and Canada have begun to see that devices of investment protection that they had created for their nationals investing abroad are now being used against them.”). One of the shifts involves the treaty provisions regarding the state of emergency. The 2004 revisions to the U.S. Model BIT, for example, added language to the emergency defense that essentially renders it self-judging, i.e., it places the sovereign in the position of determining whether a state of emergency exists. The provision now reads: “Nothing in this Treaty shall be construed . . . to preclude a Party from applying measures *that it considers* necessary for the fulfillment of its obligations with respect to . . . the protection of its own essential security interests.” U.S. Model BIT, *supra* note 248, art. 18, ¶2 (emphasis added). In the 2006 U.S.-Peru Free Trade Promotion Agreement, this provision was accompanied by a note that left little doubt about its self-judging nature: “For greater certainty, if a Party invokes [the “essential security” defense] in an arbitral proceeding . . . the tribunal or panel hearing the matter shall find that the exception applies.” United States-Peru Trade Promotion Agreement, U.S.-Peru, art. 22.2(b) n.2, Apr. 12, 2006, available at http://www.ustr.gov/Trade_Agreements/Bilateral/Peru_TPA/Final_Texts/Section_Index.html.

266. Cf. Burke-White & von Staden, *supra* note 27, at 287–96 (arguing that a more deferential standard of review should apply in arbitrations involving public law questions, especially in a subset of public law disputes that they term “quasi-constitutional” disputes and in which “a state’s essential interests are at stake and . . . the result of the litigation will impact the social and economic life of the state”).

convincingly argued that a certain amount of unsettledness is not only inevitable in light of the binary and dynamic character of investment treaties, but that it is in fact one of the strengths of the field.²⁶⁷ Decentralized adjudication is chaotic, but it is also dynamic. In investment arbitration, it creates the conditions for lawmaking through clashes of opposing opinions, and, in the best case, through honest assessments of earlier awards based purely on the merits of the positions advanced by other tribunals.²⁶⁸

If investment arbitration continues to grow at the current rate, the field may reach a point where centralized lawmaking is preferable over the current framework. Yet regardless of how the field evolves in the long term, at its current stage of development, as others have observed, a certain level of incoherence is natural.²⁶⁹ Even aside from the variations in investment treaties, the inconsistent interpretations of identical or similar provisions appear to reflect a deep divide within the investment community on how to balance the interests of investors and host countries.²⁷⁰ A young appeals facility created to increase coherence will be under enormous pressure to stick to its earlier decisions no matter what the costs. At this time, the investment community may be better served by an emphasis on the development aspect of lawmaking, even if this

267. Krishan, *supra* note 243, at 132 (“The essential insight here is that the norms that have governance effects are being generated through a binary, dialectical process—that of arbitration—which pits one state against one particular investor before one particular tribunal. This is a very peculiar—and perhaps unrepresentative—way of making law.”); *cf.* Qureshi & Khan, *supra* note 183, at 278 (“[I]f investment involves and is about ultimately ensuring development . . . [s]hould the goal not be constantly to facilitate the ‘development objective’ and better decisions all round, rather than pursuing a fetish for identity of interpretation?”).

268. *Cf.* Krishan, *supra* note 243, at 135 (“If the global law develops through the interactions of arbitral tribunals, that project is an indefinite one in time—time that states can utilize to internalize norms of an ultimately liberal order. It provides the gap, the time, that permits dissent and assent to play out, to fine tune the system, to leave it an unfinished and ever-evolving project.”).

269. *See, e.g.*, Paulsson, *supra* note 183, at 258 (“[T]his is a new area where the jurisprudence must and will feel its way toward consensus . . .”).

270. To some extent, these concerns are representative of more general concerns that the arbitration process is developed by, and therefore biased in favor of, Western commercial interests. *See* BORN, *supra* note 4, at 8.

emphasis comes at the expense of consistency.²⁷¹ *Ad hoc* adjudication combined with maximum transparency offers the flexibility to change course and the conditions for robust debate on the merits of specific awards.²⁷²

2. *Hierarchy and Precedent*

In the United States, the promotion of consistency is closely associated with the doctrine of *stare decisis*. Decisions from higher courts are binding on lower courts within their jurisdiction, creating what some have termed “vertical” precedent. By curtailing the discretion of lower court judges, binding precedent ensures that changes to existing rules are only made at the highest level, exercising a stabilizing effect.²⁷³ Although the highest courts are not technically bound by their own earlier rulings, they generally follow them or at least purport to do so. This norm of “horizontal precedent” aims to protect the stability of the law and the authority of the court’s judgments.²⁷⁴ The rigidity of this precedent system is softened

271. See, e.g., Donald McRae, *The WTO Appellate Body: A Model for an ICSID Appeals Facility?*, 1 J. INT’L DISP. SETTLEMENT 371, 385 (2010) (noting that from the bilateral nature of investment treaties, “[a] theory of the changing nature of investors’ rights has emerged . . .”).

272. Cf. Krishan, *supra* note 243, at 123 (“Is the indeterminacy of the system (which is intrinsic to a future-oriented normative vision of BITs and BIT arbitration) verifiably so terrifying? . . . On the contrary, a view from a position of indeterminacy can be stimulating.”).

273. See, e.g., KARL N. LLEWELLYN, *THE COMMON LAW TRADITION: DECIDING APPEALS* 20–21 (Little, Brown 1960) (discussing “legal doctrine,” including earlier case law, as one of the “steadying factors” in appellate adjudication); see also Kaplan, *supra* note 108, at 10 (arguing that binding precedent is not illusory, and has a stabilizing effect). As mentioned earlier, because the highest courts hear appeals selectively, whenever clear guidance from the highest courts is unavailable the intermediate appellate courts perform error correction as well as lawmaking functions. See *supra* note 108 and accompanying text.

274. See, e.g., *State Oil v. Khan*, 522 U.S. 3, 20 (1997) (“*Stare decisis* reflects a policy judgment that in most matters it is more important that the applicable rule of law be settled than that it be settled right. . . . It is the preferred course because it promotes the evenhanded, predictable, and consistent development of legal principles, fosters reliance on judicial decisions, and contributes to the actual and perceived integrity of the judicial process.”) (citations omitted) (internal quotation marks omitted); cf. *Lawrence v. Texas*, 539 U.S. 558, 576 (2003) (“The doctrine of *stare decisis* is essential to the respect accorded to the judgments of the Court and to the stability of the law. It is not, however, an inexorable command.”) (citation omitted);

considerably by the skills of common law jurists in “distinguishing” earlier cases.²⁷⁵

Not all well-functioning legal systems rely on binding precedent. Although Western civil law jurisdictions differ considerably in how courts treat earlier rulings, they generally reject notions of binding precedent and *stare decisis*. Instead, the status of earlier decisions (from higher courts or from the court itself) is akin to persuasive authority. In Germany, for example, with the exception of rulings by the Federal Constitutional Court, decisions by higher courts are not binding on lower courts.²⁷⁶ When deciding how much weight to give to an earlier decision, the place in the hierarchy of the court that made the earlier decision is only one of many factors to be taken into account. The most important factor is “the soundness of the supporting arguments” of the earlier decision.²⁷⁷ The Netherlands similarly has no rule of horizontal or vertical precedent.²⁷⁸ Other jurisdictions, including France, impose a strong presumption that rules that have been consistently articulated in a line of cases be followed as *jurisprudence con-*

Planned Parenthood of Southeastern Pennsylvania v. Casey, 505 U.S. 833, 864 (1992) (“[A] decision to overrule should rest on some special reason over and above the belief that a prior case was wrongly decided.”) (citations omitted).

275. See, e.g., Caminker, *supra* note 118, at 819 (“[W]hen judges care deeply about a particular legal issue but disagree with existing precedent, they often attempt to subvert the doctrine and free themselves from its fetters by stretching to distinguish the holdings of the higher courts.”); Felix Cohen, *Transcendental Nonsense and the Functional Approach*, 35 COL. L. REV. 833 (1935) (noting “the stretching or shrinking of precedents in every washing.”); Comment, *The Attitude of Lower Courts to Changing Precedents*, 50 YALE L.J. 1448, 1449 (1941) (“[Many] precedents have been rejected through the stratagem of distinguishing; others have been the subject of conscious judicial oversight. As a consequence, judicial discretion among ‘inferior’ judges is not so confined and limited as legal theorists would have it.”); see also LLEWELLYN, *supra* note 273, at 62 (“[O]nly in times of stagnation or decay does [the judicial] system even faintly resemble . . . a picture of detailed dictation by the precedents . . .”); cf. Timothy Schwarz, *Cases Time Forgot: Why Judges Can Sometimes Ignore Controlling Precedent*, 56 EM. L.J. 1475, 1475 (2007) (noting that precedent can be followed, distinguished, overruled, treated as mistaken, or ignored).

276. Alexy & Dreier, *supra* note 130, at 36.

277. *Id.* at 34–35.

278. Haazen, *supra* note 130, at 234–39.

stante.²⁷⁹ One could say that the civil law approach places a higher value on independence of judgment at all levels of adjudication.²⁸⁰ In practice, however, lower court judges in all of these jurisdictions have incentives to avoid reversal, and tend to follow the reasoning of higher courts. Thus, while binding precedent explicitly confers lawmaking authority on the higher courts, in other legal systems the incentives created by the operation of error correction often result in *de facto* vertical precedent.²⁸¹

In any legal system that values coherence and predictability, the hierarchical structure of court systems thus plays a critical role in the harmonious development of law. As was the case with error correction, the higher court's ability to reverse a decision that is out of line not only provides an avenue for remedying such a situation, but it also induces compliance by lower court judges. Centralized appellate review serves precisely those fundamental values that are said to be under siege in investment arbitration: It promotes fairness by ensuring that like cases are treated alike, increases predictability for stakeholders, and strengthens the external credibility of the decision-making institution.²⁸² It therefore makes sense

279. Philippe Malaurie, *Les Précédents et le Droit: Rapport Français*, in PRECEDENT AND THE LAW, *supra* note 130, at 139, 144–47; *see also* Kaufmann-Kohler, *supra* note 15, at 359 n.11. Several arbitration scholars have argued for adoption of this principle in investment arbitration. *See, e.g.*, Andrea K. Bjorklund, *Investment Treaty Arbitral Decisions as Jurisprudence Constante*, in INTERNATIONAL ECONOMIC LAW: THE STATE AND FUTURE OF THE DISCIPLINE 265, 270–80 (Colin B. Picker et al., eds., 2008) (discussing potential application of *jurisprudence constante* in investment arbitration); Kaufmann-Kohler, *supra* note 200, at 146–47 (suggesting that a practice of applying *stare decisis* to lines of cases could, over time, “develop . . . into customary international law”); Thomas Wälde, *Confidential Awards as Precedent in Arbitration: Dynamics and Implication of Award Publication*, in PRECEDENT IN INTERNATIONAL ARBITRATION, *supra* note 200, at 113, 115 (“cumulative arbitral jurisprudence in the field of investment arbitration could be said to crystallize into ‘settled jurisprudence’ . . .”).

280. There are also jurisdictions, such as China and the former communist states in Central and Eastern Europe, in which precedent has not been part of the legal tradition at all. Ewoud Hondius, *General Report*, in PRECEDENT AND THE LAW, *supra* note 130, at 1, 7.

281. *See supra* notes 127–132 and accompanying text.

282. Schauer, *supra* note 260, at 595–602; Caminker, *supra* note 118, at 850–54; *cf.* Franck, *supra* note 25, at 63 (“Inconsistency tends to signal errors, lends itself to suggestions of unfairness, creates inefficiencies, and generates

that academics and practitioners who are concerned about the effects of inconsistent awards in investment arbitration have set their sights on a permanent appeals facility as the best solution.

Yet it is conceivable that horizontal coordination could develop in investment arbitration without the looming threat of reversal by a higher-ranked adjudicator.²⁸³ While “soft” precedent does not necessarily result in consistent awards, a growing consensus may arise on many issues.²⁸⁴ Investment arbitrators operate in a relatively transparent environment, and the awareness that their awards will likely be published creates incentives to avoid the appearance of arbitrariness. For investment arbitrators, past awards are a logical place to seek guidance or, at the very least, find a useful point of reference in the absence of sufficiently specific language in investment treaties. Indeed, investment arbitration tribunals increasingly cite to earlier awards.²⁸⁵ Some commentators have suggested that a more fluid precedent system is emerging, in the sense that arbitrators justify their decisions in light of relevant awards.²⁸⁶

difficulties related to coherence, most notably a lack [of] predictability, reliability, and clarity.”).

283. Martin Shapiro has argued that “horizontal coordination” in the sense of communication between state courts may explain the largely parallel development of “common law” areas, such as tort law, in different states. See Martin Shapiro, *Towards a Theory of Stare Decisis*, 1 J. LEG. STUD. 125, 130–34 (1972), reprinted in SHAPIRO & STONE SWEET, *supra* note 261, at 102, 107–11.

284. James Fry, who calls for a shift of focus from a pure precedent approach to decision-making based on an examination of the reason or reasonableness of prior decisions, argues that a reason-based approach “would add a large measure of consistency to the regime, regardless of whether different lines of precedent develop over time.” James D. Fry, *Regularity Through Reason: A Foundation of Virtue for International Arbitration*, 4 CONTEMP. ASIA ARB. J. 57, 82 (2011).

285. Kaufmann-Kohler, *supra* note 15, at 368–73; Laird & Askew, *supra* note 183, at 298–99; Barton Legum, *Visualizing an Appellate System*, in CURRENT ISSUES, *supra* note 3, at 121, 128; but see Fry, *supra* note 284, at 63–75 (describing diverging approaches of investment arbitration tribunals to precedent).

286. See, e.g., Judith Gill, *Inconsistent Decisions: An Issue to Be Addressed or a Fact of Life?*, in CURRENT ISSUES, *supra* note 3, at 23, 27 (concluding that some degree of inconsistency is “a fact of life” but expressing the expectation that debated issues will become more settled over time); Paulsson, *supra* note 183, at 253 (predicting a “process of natural correction” in investment arbitration awards through “the consolidation of dominant trends; the contin-

And although nobody maintains that earlier awards should have the status of binding precedent in the common law sense, some tribunals have suggested that some deference may be warranted. One tribunal, in an award rendered in 2007, noted the role of investment arbitrators in developing coherent law and seemed to endorse at least a weak form of precedent:

The Tribunal considers that it is not bound by previous decisions. At the same time, it is of the opinion that it must pay due consideration to earlier decisions of international tribunals. It believes that, subject to compelling contrary grounds, it has a duty to adopt solutions established in a series of consistent cases. It also believes that, subject to the specifics of a given treaty and of the circumstances of the actual case, it has a duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law.²⁸⁷

The annulment committee in the *Enron* case similarly stated that tribunals should aim to achieve coherence. It contrasted this responsibility with the constraints that limit the role of annulment committees:

[T]he role of an *ad hoc* committee is a limited one, restricted to assessing the legitimacy of the award and not its correctness. . . . The annulment mechanism is not designed to bring about consistency in the interpretation and application of international investment law. The responsibility for ensuring consistency in the jurisprudence and for building a coherent body of law rests primarily with the investment tribunals. They are assisted in their task by the develop-

ued isolation of perplexing outliers among awards; and thus, quite simply, more consistent awards.”); *see also* Kaufmann-Kohler, *supra* note 15, at 358 (describing different possible definitions of “precedent”); *but see* Bucher, *supra* note 183, at 287–88 (noting that the absence of hierarchy among *ad hoc* decisions and lack of binding force results in uncertainty).

287. Saipem S.p.A. v. The People’s Republic of Bangl., ICSID Case No. ARB/05/7, Jurisdiction and Recommendation on Provisional Measures, ¶ 67 (Mar. 21, 2007).

ment of a common legal opinion and the progressive emergence of ‘*une jurisprudence constante*.’²⁸⁸

On the other hand, the notion of precedent in the arbitration context is not unproblematic. In arbitration, parties entrust a particular tribunal with the resolution of an identified dispute. This principle is at odds with the notion that a tribunal is bound by awards in other disputes, simply because they were issued earlier. Indeed, the ICSID Convention provides that awards are binding only as to the parties to a dispute and have no third-party effect.²⁸⁹ And some tribunals have expressed discomfort with the notion of precedent. One tribunal, in an award rendered in 2004, stressed the importance of doing justice in the case before it, noting that “in the end it must be for each tribunal to exercise its competence in accordance with the applicable law. . . . Moreover there is no doctrine of precedent in international law, if by precedent is meant a rule of the binding effect of a single decision.”²⁹⁰ At the same time, however, tribunals are not authorized to do justice in a vacuum. Arguably, in applying open-ended provisions in investment treaties, arbitrators have to take into account what meaning the relevant actors attach to these terms. The interpretation of earlier tribunals plays a role in shaping the contours of substantive rights.

A fuller exploration of the desirability of precedent in investment arbitration must wait until another day. For now, suffice it to say that the lack of consensus among investment tribunals regarding precedent not only reflects the different legal backgrounds of the arbitrators.²⁹¹ It also points to some respects in which a private dispute resolution mechanism is an uneasy fit for the harmonious development of public law.

288. Enron Annulment Decision, *supra* note 32, ¶ 65.

289. ICSID Convention, *supra* note 25, art. 53, ¶1. Some investment treaties also state that there is no binding effect between arbitration awards. See Laird & Askew, *supra* note 183, at 298–99 & n.39 (citing NAFTA Article 1136 and comparing it with Article 59 of the Statute of the International Court of Justice).

290. Société Générale de Surveillance S.A. v. Republic of the Phil., ICSID Case No. ARB/02/6, Objections to Jurisdiction, ¶ 97 (Jan. 29, 2004).

291. Barton Legum, *The Definitions of “Precedent” in International Arbitration*, in PRECEDENT IN INTERNATIONAL ARBITRATION, *supra* note 200, at 5, 6.

3. *Legitimacy in Private Adjudication*

Whether appellate review could achieve greater consistency in investment arbitration depends, in large part, on the degree of comprehensiveness of the solution. In investment arbitration, there are at least two issues that could undermine the legitimacy of rulings from an appeals facility.

The first legitimacy problem is a systemic one. It is virtually impossible to establish a comprehensive appeals facility under the current framework. As a technical matter, it is impractical to create an appeals facility within ICSID because amendment of the ICSID Convention requires ratification by all contracting states.²⁹² Recognizing this problem, the solution suggested by the ICSID Secretariat was to create an additional ICSID appeals mechanism to which sovereigns could subscribe.²⁹³ A problem with this solution, and with any “opt-in” regime, is that *ad hoc* tribunals that do not face the threat of being overturned have no reason to accord deference to awards from the appeals facility. An ICSID appeals system would also be incomprehensive in another way. Because most BITs give investors a choice between different arbitration options, investors could circumvent rulings from an appeals facility simply by bringing a claim in a different forum. As a result, arbitrators who are not regularly appointed in ICSID cases would have an incentive to deviate from rulings from an appeals facility that are viewed as pro-host state. This would hurt the development of investment arbitration law, because these institutions privilege confidentiality over transparency. A flight to other arbitration institutions, therefore, could result in more and more investment arbitration disputes and awards being hidden from view.²⁹⁴ State defendants in ICSID pro-

292. ICSID Convention, *supra* note 25, art. 66; ICSID Secretariat, *supra* note 189, at 2, *see also* Bucher, *supra* note 183, at 290–91; Tams, *supra* note 35, at 12–13 (suggesting that getting all states to ratify an amendment establishing an ICSID appeals mechanism would be prohibitively difficult).

293. ICSID Secretariat, *supra* note 189, Annex at 1–3; *see also* Franck, *supra* note 3, at 1625 (suggesting that an appeals facility could be created by adding a separate optional protocol to the ICSID Convention); Tams, *supra* note 35, at 13.

294. American legal scholars have pointed out that the growth of arbitration and other types of alternative dispute resolution poses a problem for the development of law in some areas. Specifically, this development has brought certain types of cases from the reach of public adjudicators, result-

ceedings similarly could avoid some of the precedential effects of decisions from an appeals facility by not agreeing to the appeals process and forcefully arguing that rulings from a facility they have not agreed to lack binding force.

The second legitimacy problem arises from the perspective of the parties to a particular dispute. In ICSID arbitrations, the default rule is that each party appoints an arbitrator, and the parties try to reach agreement on the chair.²⁹⁵ As noted by Jan Paulsson, a permanent appeals facility appointed by ICSID or contracting states “is in fact unlikely to have greater moral authority than the first-level tribunal. Every annulment decision is a repudiation of the award made by the arbitrators chosen by the parties (or in accordance with their agreement).”²⁹⁶ Decisions that overturn the awards of a panel appointed in accordance with the parties’ wishes will render the system more vulnerable, and increase the risk that investors and sovereigns opt out of the system. If investors perceive an ICSID appeals facility to be sovereign-friendly, they will make use of other fora made available in investment treaties, and pursue arbitration with other institutions.

Governments that do not perceive investment arbitration to be legitimate may also respond in ways that are detrimental to the development of international investment law as a “system.” They could simply refuse to comply with an award, as Argentina has done. They may also take more drastic steps: Bolivia and Ecuador have taken steps to withdraw from ICSID,

ing both in decreased lawmaking in these fields and in reduced transparency. See, e.g., Peter L. Murray, *The Privatization of Civil Justice*, 91 JUDICATURE 6, 272, 274 (2008) (“The negative consequences of resolving civil litigation by party negotiation and agreement [including arbitration] are loss of potential judicial precedent as well as losses sustained by parties who are compelled to settle because of factors other than the objective merit of their cases. . . .”); Rex R. Perschbacher & Debra Lyn Bassett, *The End of Law*, 84 B.U. L. REV. 1, 28–32 (2004) (“As a private proceeding conducted out of public view, and with no precedential value, arbitration resolves disputes without contributing to the body of law and without providing information to the public.”); see also Charles L. Knapp, *Taking Contracts Private: The Quiet Revolution in Contract Law*, 71 FORDHAM L. REV. 761, 784–89 (2002). It would be ironical if similar concerns would plague investment arbitration.

295. ICSID Convention, *supra* note 25, art. 37, ¶2(b); ICSID Arbitration Rules, *supra* note 25, r.4 (outlining default procedure for appointment of arbitrators when parties fail to select them in a timely fashion).

296. Paulsson, *supra* note 183, at 258.

and Nicaragua and Venezuela have threatened to follow suit.²⁹⁷ In addition, several nations have terminated investment agreements, and Ecuador's Constitutional Court has declared the arbitration provisions of six BITs unconstitutional.²⁹⁸ An appeals process, in which the ultimate decision-makers are not selected by the parties, could exacerbate these developments.

In sum, there is a real danger that, far from fostering coherence, an appeals facility may encourage forum-shopping and the development of different lines of authority.²⁹⁹ A

297. UNCTAD, *Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims* at 1, 1 n.4, IIA ISSUES NOTE No. 2 (Dec. 2010), available at http://www.unctad.org/en/docs/webdiaeia20106_en.pdf; see also Tuck, *supra* note 187, at 905–10 (describing developments in Latin American jurisdictions threatening enforcement of ICSID awards); but see Timothy G. Nelson, “History Ain’t Changed”: *Why Investor-State Arbitration Will Survive the “New Revolution”*, in *THE BACKLASH AGAINST INVESTMENT ARBITRATION* 555–75 (Michael Waibel et al., eds., 2010) (arguing, based on a historical survey of controversial arbitrations involving sovereigns, that it is unlikely that confidence in investment treaty arbitration will be fundamentally undermined).

298. UNCTAD reports in a recent publication: “In 2008, Ecuador terminated nine BITs—with Cuba, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, Romania and Uruguay. Other denounced BITs include those between El Salvador and Nicaragua, and the Netherlands and the Bolivarian Republic of Venezuela. In 2010, Ecuador’s Constitutional Court declared arbitration provisions of six more BITs (China, Finland, Germany, the UK, Venezuela and United States) to be inconsistent with the country’s Constitution. It is possible that Ecuador will take action to terminate these (and possibly other) BITs.” *Id.* at 1 n.3. Domestic courts may further interfere with the smooth enforcement of investment arbitration awards. Argentina’s Supreme Court has held that local courts may review arbitral awards for, among other things, compliance with Argentinean public policy, even when the parties have agreed to waive the right to appeal. See Gleason, *supra* note 75, at 283–84.

299. The forum-shopping risks are not present in multi-lateral investment arrangements that do not provide a range of options. Thus, one could imagine a re-negotiation of NAFTA’s dispute resolution provisions to provide for an appeals mechanism. Brower, *supra* note 241, at 91–94; Legum, *supra* note 24, at 239 (noting the possibility of “a more modest appellate mechanism” for investment chapters in free trade agreements and investment treaties negotiated by the United States that are highly consistent and have at least one common party). Of course, while regional appeals mechanisms may increase consistency among awards governed by a particular investment agreement, they are unlikely to contribute to coherence in the larger world of investment law. See, e.g., Katia Yannaca-Small, *Improving the System of Investor-State Dispute Settlement: An Overview* 11 (OECD, Working Paper on International Investment Number 2006/1) (“The experts consulted were over-

harmful side effect may be a decrease in transparency, which is a critical condition for lawmaking. Quite possibly, investment law may ultimately develop as a legal order with some form of precedent, and an appeals facility could play a significant role in that process. However, the selection of arbitration as the method for resolving investment disputes presents serious obstacles to such a development.

D. *Complications for the Structural Design of an Appeals Facility*

The tensions between lawmaking ideals and the realities of investment arbitration come to the fore when one tries to identify features of an appeals facility that would be conducive to lawmaking. It is tempting to use the WTO appeals process as a model, as many proponents of the creation of an appeals facility have done.³⁰⁰ After all, the Appellate Body of the WTO presents an example of successful appellate review in the adjudication of international disputes.³⁰¹ Yet WTO dispute resolution differs in significant respects from investment arbitration, not least because both the substantive law governing trade in goods and the rules concerning WTO dispute settlement constitute a single multilateral arrangement.³⁰² Due to the bilateral nature of investment agreements, as well as several other issues, the success of the WTO dispute settlement system may

whelmingly of the view that, even though they were not all convinced of the objective necessity of an appeals mechanism for investor-state awards, if some countries were ready to establish one, it would be better by far to have a single mechanism.”); Tams, *supra* note 35, at 24–25 (noting that an appeals facility can only be effective if there is one single appeals facility that is competent to hear appeals in all investment disputes).

300. See, e.g., Gleason, *supra* note 75, at 273–86 (discussing the WTO appellate system and other trade-related arbitral appellate systems and arguing that they provide a model for successful appellate review that could be transposed to ICSID); Kalb, *supra* note 241, at 209–19 (drawing lessons applicable to ICSID from the WTO and NAFTA appellate structures). Indeed, one author has suggested that the WTO Appellate Body *itself* could take appeals from investment awards. David Collins, *A New Role for the WTO in International Investment Law: Public Interest in the Post-Neoliberal Period*, 25 CONN. J. INT’L L. 1 (2009).

301. Gantz, *supra* note 3, at 56–57 (noting that the WTO Appellate Body’s success is a continuing influence on the consideration of appeals mechanisms in investment arbitration, despite differences between the two fields).

302. See José E. Alvarez, *Implications for the Future of International Investment Law, in APPEALS MECHANISM, supra* note 22, at 29, 29–30 (contrasting the WTO dispute resolution regime with foreign direct investment rules).

not be indicative of how well an appeals facility would function in investment arbitration.³⁰³

As an initial matter, for lawmaking in investment arbitration to be effective, a significant number of sovereigns must elect to participate in an appeals facility. Investment treaties should also not provide the option of bringing a claim in a different arbitration forum. In addition, parties to investment arbitrations should not be able to waive the right to appeal. In commercial arbitration, where lawmaking was not at issue, a situation in which a small percentage of the parties opt for an appeals process is not problematic. After all, the appeals process would be available solely as a service to parties who wish to have the option to obtain review of the merits of an award. When lawmaking enters the picture, however, a situation in which a large percentage of parties opt out of the appeals process has consequences for the potential effectiveness of the development of consistent standards. Tribunals that adjudicate disputes between parties who opt out of the system would not be subject to the same constraints as tribunals whose awards may be appealed.³⁰⁴ They might also be less inclined to view awards from an appeals facility as having binding force, although decisions from an appeals facility would possibly be viewed as more persuasive than awards from individual tribunals. Essentially, for an appellate system to be able to succeed, a fundamental revision of how arbitration is conducted would need to be imposed on all parties. Again, this concern does not exist in commercial arbitration, where only parties who

303. See McRae, *supra* note 271, at 382–87 (arguing that the WTO Appellate Body is of limited relevance for evaluating appeals options in investment arbitration as it deals with a system of interrelated agreements and is grounded in a highly developed institutional structure); see also Legum, *supra* note 24, at 235 (pointing out that “the great majority of standing international tribunals—including the rare international appellate bodies—have issued from a single underlying multilateral agreement with very broad participation negotiated at a single point in time.”).

304. This consideration suggests that the constraining influence of appeal is the result of both the lawmaking and the error correction functions. Cf. Mann, *supra* note 240, at 220 (noting, in the context of a discussion of the possibility of increasing coherence through introduction of appellate review, that “much as the WTO Appellate Body has instilled consistency in the WTO law, it has also instilled a layer of accountability for WTO Panels that did not exist before the Appellate Body was formed. This has also achieved a much higher degree of public acceptability of the final results.”).

want to opt in to an appeals procedure are asked to re-think the method by which arbitrators are appointed.

For the same reasons, the standard of review is complicated. Presumably because of legitimacy concerns, the Secretariat proposed that an appeals facility would apply a highly deferential standard of review, namely “clear error of law.”³⁰⁵ This level of deference, however, is not conducive to lawmaking. In fact, the justification for granting appellate courts in the United States plenary review over legal determinations is precisely that a more searching standard is essential to fulfillment of the lawmaking function.³⁰⁶ Moreover, how can an appeals facility determine the existence of “clear error” in those situations in which unequivocal precedent does not yet exist?

The implementation of an appeals facility would also present structural challenges that could exacerbate its legitimacy problems. To start, there would be a clear tension between the need to appoint experienced arbitrators to the appeals facility and the interest of representation.³⁰⁷ Recent statistics from ICSID show that the overwhelming majority of investment arbitrators are nationals of Western European countries, the United States, Canada, or New Zealand.³⁰⁸ Moreover, the membership of a representative appeals facility would likely be split on controversial issues.³⁰⁹ This has direct consequences for the force of their decisions. Precedent emanating from an internally-divided appeals facility would not necessarily possess

305. See *supra* note 252 and accompanying text.

306. Oldfather, *Universal De Novo Review*, *supra* note 1, at 309 (“Universal de novo review provides appellate courts with a broad warrant to engage in lawmaking.”).

307. Cf. Paulsson, *supra* note 183, at 258 (noting that the recruitment of members of a permanent body would re-politicize investment arbitration). The WTO Dispute Settlement Understanding requires that the members of the Appellate Body be “broadly representative of membership in the WTO.” Understanding on Rules and Procedures Governing the Settlement of Disputes art. 17.3, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401; 33 I.L.M. 1226 (1994); see also Qureshi & Khan, *supra* note 183, at 275 (favorably comparing the representative nature of the WTO Appellate Body with the unrepresentative panels that often judge BIT disputes.).

308. ICSID, *supra* note 198, at 27.

309. Cf. Kalb, *supra* note 241, at 203 (“If . . . unresolved political conflicts between states are at the source of the incoherence, the appellate body would likely continue to reflect them.”).

the same claim to authority that a majority ruling from the highest court in a well-developed court system may have.³¹⁰ Without the structural backing by a larger political system and law enforcement, a deeply divided appeals facility in investment arbitration would be quite vulnerable. Of course, one could require that the appeals facility decides unanimously. Although this would force the members of the appeals facility to reach agreement, such an approach might give rise to compromise decisions, which would not necessarily foster coherence. Moreover, the community would give up the benefits of transparency and frank debate.³¹¹

Lastly, in light of the nature of the appeals facility and of the professional and financial interests of reputable investment arbitrators, granting life tenure to members of the appeals facility (and requiring that they give up on arbitrator assignments and counsel work) is neither realistic nor desirable.³¹² Instead, arbitrators would probably serve in staggered terms of, at most, three years. The kind of institutional stability that is present in the highest courts of most countries would therefore be lacking. This would place further strains on the development of consistent interpretations.

It is probably misconceived, at least at this time, to think of investment law as a “system” comparable to national and supranational legal orders. Although an appeals facility could achieve greater unity, the establishment of an ultimate decision-maker would raise the stakes and bring with it significant risks that pull in different directions. On the one hand, there is a real chance that an appeals facility may not gain the authority necessary to guide a lawmaking endeavor. This is espe-

310. Cf. Carrington, *supra* note 118, at 583 (noting that en banc hearings in which the court was evenly split “not only failed to resolve a conflict, but probably exacerbated it by finding it unresolvable.”).

311. Donald McRae contrasts the usual practice of the WTO Appellate Body, in which opinions tend to be unanimous, with the International Court of Justice, in which concurring and dissenting opinions are often expressed and used in scholarly analysis. McRae, *supra* note 271, at 382. In civil law jurisdictions, judicial decisions are typically presented as coming from the court. They do not identify how the judges voted or which judge authored the opinion, nor do they provide concurring and dissenting opinions. MERYMAN & PÉREZ-PERDOMO, *supra* note 256, at 37.

312. Cf. Gantz, *supra* note 3, at 68 (asserting that arbitrators, when not engaged in work for the appellate mechanism, would likely serve as counsel or arbitrators in investor-state disputes).

cially true so long as investors can arbitrate their disputes outside of the ICSID framework. But a successful appeals facility would also come with significant downsides. A single-minded focus on consistency and coherence comes at a high price. It is easy to paint the Argentina awards and annulment decisions as a poster child for the mess that results from incoherence. Yet it is also possible to view them as an energized interaction between some of the brightest minds in investment arbitration, trying to find the best answers to complex questions in public international law. At least at its current stage of development, the international investment community is better served by the preservation of horizontal dialogue and the flexibility to adjust.

V. CONCLUSION

The conclusions reached in this Article are counterintuitive. In national and supra-national court systems, the principal justifications for appellate structures rest on the interests of an entire legal community. The case for appellate review in investment arbitration strongly resonates with those who believe adjudicators have a role to play in the articulation of public values. The argument for providing parties to commercial arbitrations with the option to get a “second bite at the apple” is, on its face, significantly less compelling. This is not just because of the absence of lawmaking. Rather, the reason is that the error correction justification for offering appellate review in commercial arbitration is limited to a subset of users and potential users of arbitration who are concerned about the risk that comes with a one-tier process. The reason why legal systems pay for error correction is, perhaps, that it increases substantive justice and fairness of process for *all* litigants, including many who are compelled to litigate because they were named a defendant in a case over which a court assumed jurisdiction. Yet the private nature of commercial arbitration should not stop us from considering ways in which value could be added for a substantial number of parties. Conversely, the public nature of investment arbitration provides a strong reason to carefully weigh the drawbacks and risks presented by centralized lawmaking.

The analysis conducted in this Article also shows that the content of the error correction and lawmaking values is

shaped by the substantive and procedural contexts in which they operate. In turn, how the two values are balanced has implications for the form an appeals process should take. To be sustainable, any appeals system must strike a sensible balance between accuracy, diligence, and efficiency. In arbitration, appellate review will be successful only if it is carefully tailored to meet the particular combination of goals the relevant community seeks to achieve. In commercial arbitration, an appeals procedure that is not carefully designed to give meaning to error correction adds little value and will rightly be ignored by almost all parties. On the other hand, a well-thought-out appeals process could provide a ready-made alternative for those who wish to add substantive safeguards, including potential parties who currently deem arbitration too risky. In investment arbitration, an examination of how an appeals facility would function suggests that it may well undermine the very goal its proponents seek to achieve.