

## Paulsson's nirvana fallacy

(Manuel Conthe, *Spain Arbitration Review* N.º 29/2017, June 2017, p.43-60)

In January 2017, at the very end of his dissenting vote in ICSID case “Supervisión y Control S.A. v. Republic of Costa Rica” (ARGB /12/4), Joseph P. Klock, a Miami-based American lawyer appointed as co-arbitrator by the Spanish claimant and participating for the first time in an ICSID case, wrote the following:

“The arrangement whereby two of the panel members are selected by the parties to the agreement creates an uncomfortable aura of conflict which permeates, in my view, the proceedings. It creates a true ethical burden on these other two parties to separate themselves from the interest of those who have selected them to serve. I know that I have worked hard to neutralize this factor as I am sure my esteemed colleague, Co-Arbitrator Silva Romero, has done.

However, the dignity and integrity of the ICSID proceedings would be much better served by the selection of panelists from lists where the selection is made wholly by ICSID (...).

This panel was assembled in accordance with the terms of the agreement between the parties, with one panelist appointed by each of the parties and the third, by the Chair of ICSID. To the extent that ICSID has the ability to direct the composition of panels that are to arbitrate its claims, I believe that it should consider prohibiting this arrangement. Of the three of us, the only panelist who did not have an inherent conflict was Dr. Von Wobeser, and I know that both of the remaining two of us were honored to serve under his chairmanship. He also was the only panelist who did not labor under any type of conflict burden.

(...) An appointment by a party of a judge to rule on the party's claim creates an unnecessary barrier to pure objectivity, except in situations where a high degree of technical or scientific skill and knowledge of a discipline is needed. That clearly is not the case in terms of a contract dispute. If the desire is to have three judges decide an issue, then there should be three completely impartial judges appointed, judges who are not related to the parties or to their counsel. Those procedures were not in effect in this case, and if they were, perhaps the painful process of reviewing conflict could have been avoided”.

Not unsurprisingly, Mr. Klock's reflections were quickly echoed by Jan Paulsson, one of the leading international arbitrators who has advocated for years that 3-member arbitration panels be selected in their entirety by arbitration courts, with no role whatsoever for party-appointed arbitrators. Most recently, in his keynote address at the 2017 Annual Meeting of the CPR Institute, after quoting Mr. Klock's “heart-felt account”, Paulsson stated:<sup>1</sup>

“Can't we all agree that in ideal circumstances an arbitral tribunal should operate as a team, and not as three sole arbitrators cobbling together something of dubious coherence that achieves an unappealable result but does not deserve to be called ‘consensus’? If we agree [that we] want cohesive tribunals capable of producing greater quality than their individual members, aren't presiding arbitrators the captain of those teams? Why not give *them* an important role in

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<sup>1</sup> Jan Paulsson, “Shall We Have an Adult Conversation About Legitimacy?”, 2 March, 2017, keynote address at the Biltmore Hotel, Coral Gables, available on CPR's Facebook page.

the constitution of the team – perhaps identifying a number of individuals they find compatible, or complementary, and asking the parties to rank them? (This, by the way, seems to be a more likely route to diversity than to expect it from unilateral appointments by parties whose entire focus in making appointments is to win the case. The presiding arbitrator might say ‘I’m comfortable with the industrial context, but would like a member of the tribunal to be conversant with public international law; then we’ll be all set so the third member can be someone less experienced whom I believe will make a solid contribution and who merits the experience and exposure.’) Or how about each side giving the presiding arbitrator a list from which to choose each co-arbitrator on the basis of compatibility? Or even, when full confidence reigns, go all the way and allow the presiding arbitrator simply to come up with the two others, constrained by nothing except perhaps observations by the parties as to what kind of qualities or experience the case calls for?”

He added:

“I think I have heard and examined at length in writing all conceivable arguments against my suggestion that we move away from the practice of unilateral appointments as a default rule, and I challenge any one of you to a debate because I am confident that I will prevail.

I could not attend the CPR’s Annual Meeting in Coral Gables and only knew about Jan’s remarks through GAR. I admire Paulsson and know that, this not being a fight between equals, he might be likely to prevail. But, consistent with the view that I will espouse in this article about the upside of “cognitive conflicts”, I will take up the glove and argue here that, contrary to Mr. Klock’s and Paulsson’s view, in the real world there are no compelling reason to expect awards from court-appointed panels (“CA panels”, henceforth) to be better, as a rule, than those issued by panels which include two party-appointed arbitrators (“PA panels”, for short).

After reviewing briefly the reasons why parties may want to preserve their right to appoint one arbitrator, I will argue that:

- Advocates of CA panels inadvertently fall prey to what economists call the “nirvana fallacy”: they see in the occasional failures of PA panels a conclusive argument in support of an idealized system of CA panels, in which all three arbitrators not only work as equals in harmony, but devote to all the issues and arguments made by the parties their undivided attention, and discuss freely and constructively, free of biases, how their joint decision should be crafted. Such comparison between real PA panels, with the occasional practical weaknesses that we all know, and an idealized CA approach is methodologically flawed.
- The only relevant test when comparing the performance of CA and PA panels should be the expected quality of the award, not the psychological strains or “ethical burdens” experienced by arbitrators while performing their job, which are obviously to be less in the case of very cohesive arbitration teams.
- Empirical research on the performance of teams suggests –even if does not prove conclusively- that diversity of members and even cognitive conflict among them may help them deal more effectively with complex issues or tasks. CA panels, very much like any other tightly-knit cohesive groups, may suffer specific weaknesses (“groupthink”, “confirmation bias”, “free riding”, “halo effects”...) to which PA panels may be much less

exposed. Hence, in arbitration there may be merit in the practice –probably widely extended, but mostly unrecognized- of co-arbitrators taking on the “special duty” of acting as “due process guarantors”, “Ombudspeople” or “watchdogs” for heuristics or biases which may unfairly harm the party which appointed them.

- While such “special role” of party-appointed arbitrators should not be seen, as such, as a sign of partiality, but of a sensible “division of labour” within the arbitration panel, there is no denying that party-appointed arbitrator may naturally be inclined to be too sympathetic to the views of the party which appointed them. Thus, coarbitrators should make a particular effort to maintain a fully independent, impartial mind and be imbued by what, in the case of Government-appointed members of the governing bodies of public independent agencies (like Central Banks), has been called the “Beckett effect”, i.e. the realization that, once appointed, their overriding objective should be to arrive at a good decision, not to act in a partisan fashion and serve the narrow interest of the party who appointed them. In my view, this effect could be psychologically primed and reinforced in co-arbitrators by asking them to make a supplementary “neutrality pledge” in their declaration of independence and impartiality.

### **Parties’ attachment to party-appointed arbitrators**

Paulsson is not the first or only scholar critical of party-appointed arbitrators. As explained by Alfonso Gómez-Acebo in his monumental study on such figure<sup>2</sup>, the concern about the insufficient objectivity of party-appointed arbitratros is and old one and the suggestion that all three arbitrators be appointed by the arbitral institution was advocated many years ago by Hans Smit, Tom Arnold and others.<sup>3</sup> The idea is currently espoused by several prestigious arbitrators besides Paulsson, including Albert Jan Van den Berg and, in Spain, Juan Fernández-Armesto.

In spite of such traditional criticisms, though, “the scheme of a three-member tribunal with two party-appointed arbitrators appears to be the preferred one among international arbitration end-users” (i.e. parties and counsel), as confirmed in the 2012 Queen Mary’s International Arbitration Survey, where as much as 71% of in-house counsel considered unilateral party appointments as the preferred method of selecting co-arbitrators in a three-member tribunal<sup>4</sup>.

How to explain such strong attachment by arbitration end-users to their right to appoint one of the three arbitratros? Is it an irrational drive which should just be taken as a fact of life and accepted by arbitral institutions, to make arbitration attractive? Or is it based on rational or pragmatic considerations?

Before arriving at my own conclusion, I will discuss briefly the three main reasons for that empirical preference which can be found in the literature:

- An irrational “illusion of control”.
- Lack of trust in arbitral institutions
- Appreciation of the especial role of party-appointed arbitrators

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<sup>2</sup> Alfonso Gómez-Acebo, “Party-Appointed Arbitrators in International Commercial Arbitration”, Wolters Kluwer, 2016.

<sup>3</sup> Gómez-Acebo, *op.cit.*, par.3-66 and 3-67.

<sup>4</sup> Gómez-Acebo, *op.cit.* par.3-4.

## The “illusion of control”

Gómez-Acebo describes as “mental gambling” one of the reasons which may explain the special interest of parties and their counsel in appointing “their” own arbitrator:<sup>5</sup>

“Most parties and counsel in international arbitration devote some time to speculating as to what candidate to be unilaterally nominated will be better (closer or less hostile) to the appointing party’s position in the dispute. This mental gambling causes no harm to the arbitral proceeding if it is just that. Perhaps some arbitration end-users are attached to the practice of unilateral appointments because they see in that mental gambling a tool to increase their chances of winning the case, as though their choice could influence the outcome of the arbitration more than that of the other party”.

This “mental gambling” does not seem particularly rational, as both parties will have the same opportunity to appoint “their” arbitrator and, consequently, their apparent advantages will cancel out.

In my view, there is a good chance that this psychological attachment of parties to making their own choices, even if not fully rational, is really at play in arbitration, as it would be just an illustration of the phenomenon described by psychologists as “the illusion of control”.

The term was coined in the 70s by the American psychologist Ellen Langer.<sup>6</sup> In one of her most famous experiments, she made lottery tickets available for \$1 to some firm employees in Long Island. In one case, she allowed the buyers to select their own lottery number, while in the other buyers were given no choice (in fact, they were allocated exactly the same numbers chosen by the members of the first group). All subjects were subsequently approached, the morning of the lottery drawing, and asked how much they would ask for their ticket, as tickets had sold out and other firm employees were demanding theirs. As predicted by Langer, the choice manipulation had a considerable effect: while buyers who had not selected their number asked, on average, \$1.96 for their \$1 ticket, those who had chosen their own number required, on average, \$8.67. In other words, even though the chances of winning the lottery were identical in both cases, subjects irrationally attached particular value to having been able to select their own number, as if this had potential influence on the outcome.

Thus, I would not exclude that an “illusion of control” reinforces the parties’ wishes to select one of the three arbitrators. But there are at least two additional rational reasons which may justify that wish, to which I now turn.

## Lack of trust in arbitral institutions

A second explanation of why arbitration end-users may be adamant about appointing their own arbitrator is mentioned by Paulsson himself, when he describes the “Kryptonite argument” that will defeat him every time:<sup>7</sup>

“Here I show you how to win the argument: you look me in the eye and say: ‘*I don’t trust the institution*’, and so long as I can name one of the arbitrators I feel that I will reduce the risk of a runaway tribunal doing something crazy- but unappealable.

That argument is indeed made, like it or not. Decent arbitral institution cannot fail to realize that it is a disappointing and sobering message, indeed something of an indictment. They must absorb this reality, and do try to do two things about it. The Big

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<sup>5</sup> Gómez-Acebo, *op.cit.* , par.3-78.

<sup>6</sup>Ellen J. Langer, “The Illusion of Control”, *Journal of Personality and Social Psychology*, 1975, Vol.32, No.2, 311-328.

<sup>7</sup> Paulsson, “Shall We Have and Adult Conversation...”, *op.cit.*

Thing is to earn such trust that this kind of worry about a runaway tribunal evaporates. The Little Thing is far easier, and may in practical terms be just about as good. It is to focus on the involvement of the parties in the selection of arbitrators, and to attend to the numerous adaptations and refinements that may take the edge off the disadvantages of what one might call unreconstructed unilateralism”.

As I will explain later, this rationale for the right of appointing arbitrators should not be dismissed lightly, as it may be considered an effective antidote against the “nirvana fallacy”: parties may be right in assuming, conservatively, that the actual working of arbitration panels fully appointed by arbitral institutions (let alone by the presiding arbitrator) may depart from the ideal, either because members were not adequately chosen or because the dynamics within the panel made it overlook some aspects of the dispute very relevant for them. I will come back to this point.

### **The especial role of party-appointed arbitrators**

Finally, some scholars have made a positive case for party-appointed arbitrators.

The most traditional and conventional view is that they can ensure that the case presented by the party who appointed them is properly understood by all the members of the arbitral tribunal, something which cannot be taken for granted when there are cultural differences among arbitrators or parties (e.g. some coming from Common Law jurisdictions, while others having a background in Civil or Islamic Law).

But other scholars go beyond that traditional, modest argument and make the case for party-appointed arbitrators to play a “special role”. Among them, Catherine Rogers has argued that by acting as “devil’s advocates” –i.e. by systematically but constructively second-guessing the majority, and challenging it when appropriate- they can improve the tribunal’s deliberation and the quality of the award, and prevent “groupthink”.<sup>8</sup>

I share this view, for the reasons to be spelled out later on when making the case for party-appointed arbitrators. But let’s deal before with Paulsson’s “nirvana fallacy”.

### **The nirvana fallacy: the potential failures of cohesive teams**

Economists have come to realize that the existence of a “market failure” (e.g. lack of competition or the existence of externalities) is not enough to support the case for an intrusive public intervention (e.g. the nationalization of the industry or the sector). One needs to prove that the public instrument or intervention to be used or implemented, as designed and applied in practice, is likely to lead to better results than the *status quo*. As Jean Tirole, the 2014 Nobel Prize winner for Economics, has recently argued, many public interventions frequently backfire and “the road to hell is paved with good intentions”.<sup>9</sup> You cannot compare a real, suboptimal arrangement with an idealized alternative, since the latter may not be a realistic depiction of how the new alternative will pan out.

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<sup>8</sup> Catherine A. Rogers, “Ethics in International Arbitration”, Oxford University Press, 2014, Chapter 8, par. 8.51-8.69.

<sup>9</sup> Jean Tirole, “Économie du Bien Commun”, PUF, 2016, p.86-89.

It was Harold Demsetz, the famous economist from the University of Chicago, who identified such methodological failure and call it the “nirvana fallacy”:<sup>10</sup>

“The view that now pervades much public policy economics implicitly presents the relevant choice as between an ideal norm and an existing ‘imperfect’ institutional arrangement. This *nirvana* approach differs considerably from a *comparative institution* approach in which the relevant choice is between alternative real institutional arrangements. In practice, those who adopt the nirvana viewpoint seek to discover discrepancies between the ideal and the real and if discrepancies are found, they deduce that the real is inefficient. Users of comparative institutions approach attempt to assess which alternative real institutional arrangements seems best able to cope with the economic problem; practitioners of this approach may use an ideal norm to provide standards from which divergences are assessed for all practical alternatives of interest and select as efficient that alternative which they see as most likely to minimize the divergence”.

Under this view, when comparing in arbitration the dominant PA approach with the alternative CA approach is not enough to describe the occasional failures of the former –e.g. the partisanship of some party-appointed arbitrators and the way they poison the team spirit of the panel-: you need to prove that in the real world the alternative CA approach is likely to be better, using as a yardstick not the team spirit or congenial atmosphere within the tribunal –a metric in which the CA approach will naturally excel-, but the quality of the award.

In order to do so, one has inevitably to discuss the potential shortcomings of CA panels, as they would be likely to function, on average, in the real world.

This reality check is important, because, as recalled by Rogers<sup>11</sup>, modern accounts of the impartiality of arbitrators are often framed in absolute, superhuman and even mythological terms which mirror Ronald Dworkin’s myth of judge “Hercules” – an ideal judge with superhuman skill, learning, patience and acumen-. But in the real word one should not assume that, when dealing with complex cases, all three court-appointed arbitrators will be in the image of dworkinian Hercules, endowed with unmatched knowledge and unlimited time to study the case and render a perfect award.

On the contrary, a CA approach may suffer from, at least, the following weaknesses:

- A poor choice of arbitrators by the court, particularly of a chairperson who is not capable of making the team work in an effective way;
- The risk that the team becomes too cohesive and prone to “groupthink”, premature consensus or “confirmation bias”, without enough attention being paid to alternative ways of thinking or even complete disregard of key contentions made by one of the parties.
- The risk that individual arbitrators act as “free riders” and trust excessively the work of the chair or drafter, without scrutinizing critically their work. This potentially passive attitude of some arbitrators may be compounded by a “halo effect” or excessive deference to the panel member with the most prestige, particularly if he or she is acting as chair (let alone if he or she, as “captain of the team”, has nominated their fellow arbitrators, as suggested by Paulsson!).

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<sup>10</sup> Harold Demsetz, “Information and Efficiency: Another Viewpoint”, *The Journal of Law and Economics*, 12, no.1, April 1969, p.1-22.

<sup>11</sup> Rogers, *op.cit.* , par.8.01-8.04.

In the following paragraphs I will make a brief reference to some of these problems and biases which may affect particularly CA panels, and for which party-appointed arbitrators, if well chosen, may be a potentially effective antidote.

### **Groupthink and confirmation bias**

As described by Rogers<sup>12</sup>

“Groupthink is a phenomenon developed by cognitive psychologist Irving Janis. Through his research, Janis demonstrated that Groupthink is a ‘mode of thinking that people engage in when they are deeply involved in a cohesive in-group, when the members striving for unanimity override their motivation to realistically appraise alternative courses of action’. Groupthink ‘occurs when the decision-making capabilities of a panel become affected by subtle peer pressure’”.<sup>13</sup>

This is not the place to describe in detail how “groupthink” may emerge and become entrenched in very cohesive groups, but, in my view, one of the explanations of this pathology is the simultaneous effect on all its members of the cognitive bias which, subsequent to Janis’ pioneering work, has been described as “confirmation bias”.<sup>14</sup> The term is a modern one, but the phenomenon was already described in the early 17th century by British philosopher Sir Francis Bacon, when he wrote:<sup>15</sup>

“The human understanding, when it has once adopted an opinion [...] draws all things else to support and agree with it. And though there be a greater number and weight of instances to be found on the other side, yet these it either neglects and despises, or else by some distinction sets aside and rejects; in order that by this great and pernicious predetermination the authority of its former conclusions may remain inviolate”.

Bacon further wrote that “the first conclusion colours and brings into conformity with itself all that come after” - introducing the idea of what psychologists now call 'confirmation bias' or "belief persistence".

The key insight here is that very cohesive groups may be particularly prone to this cognitive mistake, as peer pressure to achieve consensus may lead members to keep for themselves information or opinions (“hidden profiles”) which may be at odds with the dominant view. As explained below, a good, inquisitive leader may be able to bring those opinions to light and prevent the emergence of “groupthink”. But, absent such enlightened chair, the group will lack the automatic system of “check and balances” which will be present spontaneously in less cohesive groups, like PA panels, where unanimity is not the overriding goal.

### **Free riding**

The idea that in a team of three people chaired by one of them –who is frequently expected to draft the award- all three members will work as hard in studying submissions and checking the accuracy and completeness of awards is, in many cases, a far cry from reality: the chairperson will take frequently the brunt of the work, provide the first sketch of the award and organize and structure the debates of the panel.

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<sup>12</sup> Rogers, *op.cit.*, par.8.53.

<sup>13</sup> The source of Rogers’ quotation is Irving L. Janis, “Victims of Groupthink”, Houghton Mifflin, 1972.

<sup>14</sup> Raymond S. Nickerson, “Confirmation Bias: A Ubiquitous Phenomenon in Many Guises”, *Review of General Psychology*, Vol.2 No.2, 175-220 (1998).

<sup>15</sup> Francis Bacon, “Novum Organum”, Book I, 109 point 46 (1620).

This may –and actually does- also happen in PA panels, but in those panels party-appointed arbitrators have an incentive to check the accuracy and soundness of any findings which run against the interests of the party which appointed them. Thus, they may be more selective in their “free riding” and, in so doing, protect the legitimate interests of both parties against the potential mistakes of a non-Herculean chair.

### **Halo effect and hierarchies**

The “halo effect” is the phenomenon whereby we assume that because people are good at doing A they will be good at doing B, C and D, even if the tasks are unrelated. The term was first coined by Edward Thorndike, a psychologist who used it in a 1920 study to describe the way that commanding officers rated their soldiers: he found that they usually judged their men as being either good or bad right across the board, with very few soldiers being said to be good in one respect but bad in another. In business, economist Phil Rosenzweig claimed that it is at work in the attitude taken by journalists and consultants with respect to companies and business leaders: when a company is growing and profitable, they tend to infer that it has a brilliant strategy, a visionary CEO, motivated people, and a vibrant culture. But as soon as performance falters –even for reasons unrelated to the company-, the same journalists and consultants are quick to declare that the strategy was misguided, the CEO became arrogant, the people were complacent, and the culture stodgy.<sup>16</sup>

For the same reason, the prestige and international recognition of an arbitrator may well lead to his/her appointment as chairperson of a panel. Now, as the recognized group leader, he or she will be “given control over decisions and allowed to direct others’ action, whereas lower ranked individuals are expected to defer to others and keep their opinions to themselves”.<sup>17</sup> This internal hierarchy, in turn, may induce lower ranked arbitrators to be shy and reticent to challenge the chair’s views.

Party-appointed arbitrators may find themselves in the same predicament, particularly when confronted with a dominant or very prestigious chair. But chances are that the origin of their appointment, and the incentive not to leave their party in the lurch, may offset any “halo effect” and prompt them to hold their ground if they strongly feel that the dominant panel’s view is wrong or unfair.

### **The case for cognitive tension within a deliberative group**

Social psychologists and, in general, experts on the dynamics and performance of teams and social groups make a crucial distinction between two different types of “conflict” among their members:

- “Cognitive conflict” (also described as “task conflict”), i.e. discrepancies or differences of opinion among members on how to approach a task or deal with an issue or problem.

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<sup>16</sup> Phil Rosenzweig, “The Halo Effect..and the Eight Other Business Delusions that Deceive Managers”, Free Press, 2007.

<sup>17</sup> Cameron Anderson and Jessica A. Kennedy, “Micropolitics: a New Model of Status Hierarchies in Teams”, pg. 54 in “Looking Back, Moving Forward: A Review of Group and Team-Based Research”, edited by Margarete A. Neale and Elizabeth A. Mannix, Emerald, 2012.



- “Affective conflict” (also called “relationship conflict”), i.e. personal animosities, mistrust or bad feelings among members.

Cognitive conflicts are generally deemed to help the group be creative, thorough and good-performing, while affective conflicts prevent teams from working effectively. Concerning the first type of conflict, i.e. the potential “good conflict”, three management experts wrote:<sup>18</sup>

“Under some circumstances conflicts may be beneficial for organizational workgroups (...). Empirical research on conflict within organizational workgroups and teams shows that moderate levels of conflict are positively related to teams’ innovation level. Furthermore, studies have suggested top management team (TMT) decision making may benefit from conflict. A sociological study among scientists suggested that those scientists experiencing conflicts with colleagues about how to approach their task were more productive than those scientists who did not experience such conflict”.

It is then obvious that the key for a team to deal successfully with a complex task is twofold:

- First, to stimulate and protect the diversity of views among members; and
- Second, to prevent “cognitive conflicts” (i.e. intellectual discrepancies) from morphing into “affective conflicts” (i.e. strained personal relations).

There are several techniques to do so.

### **The role of the chair: the “Rubin method”**

Among listed companies around the world it is now generally considered best practice that “the chairman of the board of directors, as the person responsible for its proper operation, ensures a good level of debate and the active involvement of all members, and safeguards their rights to freely express and adopt positions”.<sup>19</sup> (emphasis added)

Robert Rubin, the former Goldman Sachs executive and Secretary of the Treasury, is probably the epitome of such enlightened way of chairing a group. As he reminisces in his memoirs of his years at the head of the Treasury:<sup>20</sup>(emphasis added)

“From his own staff, [President Clinton] expected candor, and my approach was to tell him what was on my mind –though in some cases diplomatically. Clinton specifically told us during our Little Rock transition meeting. ‘If you don’t tell me what you really think, I’m dead’.

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<sup>18</sup> Karen A. Jehn, Sonja Rispens and Sherry M.B. Thatcher, “Managing Conflict in Groups and Teams: Conflict about Conflict”, in the collective book edited by Margaret A. Neale and Elizabeth A. Mannix “Looking Back, Moving Forward: A Review of Group and Team-Based Research”, Emerald, 2012, p.135.

<sup>19</sup> In Spain, this recommendation, originally included in its 2006 Code of Good Corporate Governance for listed companies, became mandatory in 2014 when it became part of article 529 sexies of Spain’s Capital Companies Act.

<sup>20</sup> Robert E. Rubin, “In An Uncertain World. Tough Choices from Wall Street to Washington”, Thomson-Textere, 2003, p. 134.

The comment reminded me of what John Weinber had once said to me at Goldman Sachs: as a CEO, you have a special place in the minds of your subordinates. People in your own organization have a natural tendency to pull their punches around you, to soften the bad news and try to tell you what they think you want to hear. Because you're a bit of a King, you can easily get an unrealistic sense of the wisdom of your own views and your merits as a leader. (Walter Mondale once told me that when he was Vice President and his party's presidential nominee, everyone laughed uproariously at his jokes. Then he lost the election and realized he wasn't so funny after all.). To keep a realistic sense of yourself and to make well-informed decisions, you have to go out of your way to make people feel comfortable disagreeing with you".

That Rubin walked the talk and went out of his way to make people feel comfortable when disagreeing with him is confirmed but his then subordinate and subsequently Treasury Secretary himself, Timothy Geithner:<sup>21</sup>(emphasis added)

"Rubin was the former head of Goldman Sachs, but he was self-deprecating and funny, demanding without Larry [Summers]' rough edges. He believed in good process. He wanted input from all his advisers no matter where we were in the hierarchy, even if we disagreed with –especially if we disagreed with him. He was calm, dispassionate, and almost comically deliberate, analyzing problems from every possible angle, scribbling down risks and probabilities on his yellow legal pad, gathering information and 'preserving optionality' until he absolutely had to decide.

### **The upside of diversity in membership**

Besides an enlightened attitude of the group's leader, diversity in its composition may also frequently favour good performance, particularly when dealing with complex tasks. As two management experts put it:<sup>22</sup>

"The effects of diversity are complicated. The preponderance of evidence supports the notion that diversity benefits group performance under specific circumstances, yet even then, it must be carefully managed. The benefits of diversity are more likely to accrue when groups are facing complex, nonroutine tasks in which the aggregation of unique information and perspectives is necessary or creativity and innovation are needed".

In a recent book in support of "messy procedures", British economist Tim Harford echoes the conclusions of recent research on the performance of teams:<sup>23</sup>

"When experimental subjects are challenged to write an essay, they write better, more logical prose when told their work will be read by someone with different political beliefs rather than someone like-minded (...). When deliberating with a group, then, we should be seeking out people who think differently, who have different experiences and training, and who look different. Those people may bring fresh and useful ideas to the table: even if they do not, they'll bring out the best in us- even if only by making us feel awkward and forcing us to shape up. That messy, challenging process is one we should embrace".

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<sup>21</sup> Timothy F. Geithner, "Stress Test. Reflections on Financial Crises", Crown Publisher, 2014, p.45-46.

<sup>22</sup> Katherine W. Phillips and Evan P. Apfelbaum, "Delusions of Homogeneity: Reinterpreting the Effects of Group Diversity", in "Looking Back, Moving Forward...", *op.cit.* , p.189.

<sup>23</sup> Tim Harford, "Messy: The Power of Disorder to Transform our Live", Riverhead Books, 2016, p.49.

It is true that courts and presiding arbitrators may indeed look for, and achieve, diversity when appointing an entire panel. But, in my view, giving the parties a role in appointing some of the arbitrators may enforce diversity in a more effective and certain manner.

### **Diversity of roles**

Finally, the performance of decision-making groups can also be improved by the use of techniques which do not rely on the behavior of the chair or the make-up of the group, but on the allotment of specific roles to its members.

One clever approach is the “six thinking hats method” (or “parallel thinking”), invented by the Maltese management guru Edward de Bono.<sup>24</sup> It requires the entire group to alternate, at the prompting of its leader, between different “hats” or mental attitudes (i.e. the “yellow hat”, which requires to look at the strengths of an idea; the “black hat”, which focuses on its weaknesses; the “green hat”, on potential improvements...). To the extent that all members of the group are asked to wear the same hat and share the same attitude at any single time, this method allows teams to analyze problems from all possible angles, without any scope for conflict among their members, as they think “in parallel”.

But probably the method with the longest tradition is the allocation of different roles to individual members of the group, with one of them being commissioned to challenge the dominant views of the group and play “devil’s advocate”.

As Rogers recalls, this was the method advocated by Janis to fight “groupthink”:<sup>25</sup>

“The most effective way to reduce the prevalence of Groupthink, according to Janis, is to insert into a tight-knit group certain individuals whose assigned function is to challenge the consensus of that group. The function of this person is to serve as what Janis calls the ‘devil’s advocate’, meaning someone who systematically and intentionally argues for a position contrary to whatever position is being advocated or contemplated within the group. Janis proposes that this role be formally designated and that the position be rotated among group members at each meeting. This is the justification, for example, for shareholder-nominated directors. Proponents of shareholder-nominated directors argue that they can break through Groupthink because they have different interests and alliances than the other corporate officers on the board. Similarly, on an arbitral tribunal, arbitrators who are appointed by the parties are essentially identified because of a perceived propensity to look sceptically and question decisions that may have negative consequences for the party who appointed them”.

Rogers adds:<sup>26</sup>

“The ideal party-appointed arbitrator is someone who can argue forcefully to check the majority’s positions that are in opposition to those of the appointing party, but in a ‘low key’ that does not seem overtly partisan. By systematically but constructively second-guessing the majority, and expressly challenging it when appropriate, party-appointed arbitrators can improve the process, within tribunal deliberations, in the process of drafting the award and by, in some cases, actually writing a dissent. Several commentators have offered anecdotal explanations of how party-appointed arbitrators contribute to deliberative functions on the tribunal. Most such explanations, however, are often offered by way of

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<sup>24</sup> Edward de Bono, “Six Thinking Hats”, Little Brown and Company, 1991.

<sup>25</sup> Rogers, *op.cit.*, par.8.57.

<sup>26</sup> Rogers, *op.cit.* par.8.60-8.61.

apology for historical practices or justification for a party's preferences. These accounts provide important real world verification of the value of deliberations in which party-appointed arbitrators press against a Groupthink-gravitational pull to the path of least resistance.

Under this view, party-appointed arbitrators are not a necessary evil that must be tolerated to make parties feel comfortable or because there are not viable alternatives. They are, instead, an important structural feature of international arbitral tribunals. The threat and potential reality of publishing a dissent is part of this process of challenge that promotes accountability. It can also promote party confidence in a process that lacks any form of appellate review, and is regarded as creating some potentially perverse incentives for overly eager agreement by arbitrators with co-panelists in order to secure future appointments".

Gómez-Acebo, who accepts a special role for party-appointed arbitrators as "cultural translators", has nonetheless serious misgivings about the idea of party-appointed arbitrators as "devil's advocates". He sees in such idea two serious sources of imbalances. First, if one party-appointed arbitrator takes on that special role, but the other does not and considers his or her role to be identical to the presiding arbitrator's, the latter may be at a disadvantage. Additionally, even if both party-appointed arbitrators take a special role, "the smarter or more hard-working a party-appointed arbitrator, as compared to the other party-appointed arbitrator, the better the position of the party who appointed that arbitrator might be in comparison to the other party".<sup>27</sup>

I essentially agree with Rogers and do not share Gómez-Acebo's qualms about the "special role" of party-appointed arbitrators.

In an ideal world, all three arbitrators should play an identical role and act in a fully symmetrical way. In real practice, however, arbitrators work under very significant constraints and frequently apply the principle of division of labour.

Thus, for instance, if the contract is subject to the law of country X and only one arbitrator is a citizen of this country, the chances are that he/she will take a special role in advising their colleagues on recent jurisprudence applicable to the case. Similarly, if the case requires financial calculations and one of the arbitrators has a strong background in finance, it may be natural that the president asks him/her to prepare the first draft of the relevant paragraphs of the award. Now, in a world of "bounded rationality" and time constraints, how can the arbitration panel make sure that the arbitration procedure and the award are fair to both parties, have respected fully their due process rights and taken into account all their relevant arguments? One natural approach is for each party-appointed arbitrator to act not as that party's "advocate", but as its "due process watchdog", "monitor" or "Ombudsperson".

This is important, because in very complex arbitration cases there is always a critical moment when the arbitral tribunal will take a final view on each contentious issue, and it will be loath to change it thereafter. Now, if at that particular juncture the tribunal overlooks one key argument made by one of the parties, the final decision may be to that party's disadvantage. Thus, it is important that party-appointed arbitrators make sure that no relevant arguments of their parties are overlooked at such critical time.

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<sup>27</sup> Gómez-Acebo, *op.cit.* , par.5-20 through 5-25.

In an ideal world all three arbitrators should make their greatest effort to retrieve the key arguments from either party, so that all are duly considered before the final decision is reached. But in the real world, it may be expedient and practical for the tribunal to divide tasks, so that party-appointed arbitrators implicitly focus on the arguments made by the parties which appointed them. For the presiding arbitrator this arrangement will be convenient: if when deciding against one of the parties none of the wing-arbitrators raise any convincing objection or red flag, the chair may feel reassured that the decision is right and well founded.

What if, to consider Gómez-Acebo's concern, one of the party-appointed arbitrators is more hard-working, experienced or knowledgeable than the other? Might this not put one of the parties at a disadvantage?

It might, indeed, but there is nothing wrong with that: this will give the parties the incentive to look for hard-working arbitrators, who understand the issues, study them hard, and, when appropriate, hold their ground and stand up for their views when they consider that the majority is wrong.

### **Enhancing impartiality: priming the “Beckett effect”**

As it should be apparent from my remarks so far, I do not think Joseph Klock is right in equating party-appointment with lack of impartiality. If that link were inevitable, then:

- Justices of the US Supreme Court could not be impartial vis-a-vis their Government, as they are appointed by the US President.
- Members of the executive board of the German *Bundesbank* could not be independent from their Government, as they are appointed by the Chancellor.
- And European Commissioners could not act independently from the Government of their country of origin, since they were originally nominated by them.

In other words, there are many independent institutions around the world in which some key senior officials are nominated or appointed by Governments, but are nonetheless required to act in office in a fully independent and impartial manner. They are in exactly the same position as party-appointed arbitrators with respect to the party which appointed them.

But there is no denying –and here Joseph Klock is right- that any party-appointed arbitrator may spontaneously be inclined to be too sympathetic to the views of the party which appointed him/her. This is inevitable, because, as American consultant Robert Cialdini claims, the “law of reciprocity” is one of the drivers of human behavior, and makes us grateful to anyone who has done us a favour (like appointing us to an important –and well-paid!-arbitration case).<sup>28</sup>

How can party-appointed arbitrators control their natural inclination to be grateful towards the party which appointed them?

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<sup>28</sup> Robert Cialdini, “Influence. The Psychology of Persuasion”, 5th ed. 2008, Chapter 2. See also Robert B. Cialdini, Noah J. Goldstein and Steve J. Martin, “YES! 50 SECRETS FROM THE SCIENCE OF PERSUASION”, 2007, p. 5 and 38-41 and Manuel Conthe and Antonio Delgado, “Conflicts of Interest and Disclosure Duties of Non-Martian Arbitrators”, World Arbitration and Mediation Review, Vol.8, No 1, April 2014.

This issue has long been identified and debated in the German Central Bank (*Bundesbank*), which has always been proud of its independence *vis a vis* the Government, notwithstanding the fact that every member of its Council is appointed by the Government, and that often their President and Vice-president have previously served as senior Government officials- e.g. as Secretary of State for Finance or Chief Economic Advisor for the Chancellor-.

An old member of the Council of the *Bundesbank*, professor Otmar Issing, coined the term "Beckett effect" to describe the spirit of independence felt by those appointed by the Government to become members of an independent institution like the Central Bank. In a famous speech in 1991, he expressed the idea as follows:<sup>29</sup>

"The influence, prestige and the task entrusted to the Central Bank can produce in the newly arrived a transformation in his perception which can provoke in some cases surprise and frustration, and even indignation, towards his political sponsor. I would call that phenomenon "Beckett effect", remembering the experience of Henry II of England when he designated his trusted Chancellor as the Archbishop of Canterbury, and saw how the assumed representative of the King's interests transformed himself into a genuine defender of the interests of the Church. I won't say whether [the effect] also requires a disposition to suffer martyrdom".

The "Beckett effect" is necessary in all independent institutions and in all those people entrusted to exercise a role with impartiality. It is true that such effect is not spontaneous or natural, as it may be seen as contrary to our spontaneous human inclination to be grateful to, and reciprocate, those who did us a favour. For that reason, modern arbitral institutions could take a cue from past practices, like the 1868 Arbitration Convention between Mexico and the United States, which –as reported by Gómez-Acebo- required that party-appointed commissioners “shall, before proceeding to business, make and subscribe a solemn declaration that they will impartially and carefully examine and decide, to the best of their judgement, and according to public law, justice, and equity, without fear, favor, or affection to their own country” (emphasis added).<sup>30</sup>

Thus, adding to the standard declaration by party-appointed arbitrators the final pledge that they will act “without fear, favor, or affection to the parties, and especially to the party which appointed me” might be a practical way to prime in their minds the “Beckett effect” and ensure that, even if they take the special role of “ombudsperson” for that party, they will discharge their duties in full impartiality.

## **Concluding remarks**

If we use the only relevant yardstick in arbitration -the quality of the award and the procedure-, there are no *a priori* reasons to think that arbitration panels appointed in their entirety by arbitral institution (CA panels) will outperform those in which two of the arbitrators were appointed by the parties (PA approach). Whether arbitrators enjoyed their experience and felt part of a well-knit, cohesive team or, on the contrary, suffered the personal anguish and “ethical burden” mentioned in Joseph Block’s dissenting opinion is immaterial: the only relevant metric is to what extent the panel produced a good award, i.e. to what extent the award applied correctly the law and took into account all the relevant arguments and facts alleged by the parties.

Jan Paulsson’s implicit view that “cohesive tribunals” equals “greater quality award” seems to me a fallacy, as it overlooks the potential downside of “cohesion” in a world of non-Herculean

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<sup>29</sup> Otmar Issing, “Geldpolitik im Spannungsfeld von Politik und Wissenschaft”, speech in a round table in tribute to Professor Norbert Klöten, Stuttgart, 15 March 1991.

<sup>30</sup> I take the quote from Gómez-Acebo, *op.cit.*, par.2-29.

Court-appointed arbitrators. Under ideal circumstances, both PA and CA panels may work effectively; and, in the real world, either one may also show occasional shortcomings, even if the arbitration literature has focused exclusively on the risk of partisanship of party-appointed arbitrators.

It is true, though, that, even if there is no clear-cut case for doing away with party-appointed arbitrators, there are potential measures which could improve PA panels and minimize their potential shortcomings.

In his address at Boca Ratón, Paulsson himself suggested that, before appointing any arbitrator, the lawyers from the two parties talk to each other and say: “If I appoint A, whom will you appoint? Are you saying B? Oh, no, then I’d appoint C. What’s that, you like A? Well then, think of someone other than B”. This is a clever suggestion, since this prior coordination would allow Claimant to escape the inevitable “prisoner’s dilemma” that it typically will face when choosing its wing-arbitrator: if it chooses an extremely impartial, enlightened, fairly-minded one, it runs the risk that Respondent does not “cooperate” and appoints a strongly partisan one. Hence, lest it ends up playing “sucker”, Claimant will be tempted to take the uncooperative route and be partisan in its choice. As in all prisoner’s dilemmas, *ex ante* cooperation and coordination between the players may allow them to move from their third to their second-best.

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But one can think of many other measures.

For instance, to impress on party-appointed arbitrators the overriding need to remain impartial, arbitral institutions could:

- Include in their declaration of independence and impartiality a specific reference to their impartiality vis-a-vis the party which appointed them.
- Forbid, once the panel is formed, any *ex part* communication by arbitrators, making any such behavior cause for immediate dismissal.

Probably as important, chairpersons should learn and apply best practices on how to lead arbitration panels and harness the energies of party-appointed members in the most productive way. Two specific suggestions come to mind:

- First, chairpersons should make their utmost to prevent “cognitive/task conflicts” (i.e. disagreements) from transforming into “personal/relationship conflicts” (i.e. personal animosities). One of the most effective ways to do so will be for the chairperson, as leader of the team, to accept, and even stimulate, alternative, critical ways of thinking and “get out of their way to make colleagues feel comfortable when disagreeing with them”.

My guess is that if presiding arbitrators would systematically follow “Rubin’s method” – without necessarily going to the extreme of being “comically deliberative”-, panels would be more effective and the occasional problems resulting from party-appointed arbitrators, much less frequent.

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<sup>31</sup> For the classical application of game theory and the prisoner’s dilemma to legal problems, see Douglas G. Baird, Robert H. Gertner and Randal C. Picker, “Game Theory and the Law”, Harvard University Press, 1994, particularly p.32-33. They illustrate the prisoner’s dilemma with the case of two landowners that, in order to keep flood waters off their land, can build levees, which will be costly and, while protecting them, will aggravate the risk of flooding for their neighbour. They will be better off if both refrain from building them. But unless they talk and coordinate, chances are they will build them, at a net loss for both. If you substitute “partisan arbitrator” for “levee”, the parallel is immediate.

- Second, a clear distinction should be drawn between “dissenting opinions” (i.e. texts written by the dissenter explaining the reasons why it cannot support the majority decision) and “dissenting votes” (i.e. the mere expression in the award that a specific decision was not unanimous, as one of the arbitrators voted against). While dissenting votes may occasionally be inevitable and just reflect different but legitimate views among arbitrators, dissenting opinions, particularly those lengthy and passionate ones, are almost always a sign of failure. On many occasions the dissenter will probably be the only one to blame. But the need for dissenters to write opinions (as opposed to cast dissenting votes) can some times be arguably traced to the chair’s inability or unwillingness to spell out in the award, in a fair and deliberative manner, the merits of the two conflicting arguments at hand, and why in the end a majority of arbitrators, after gauging their relative strength, were swayed by one of them. In the absence of such explanation, the dissenter, unwilling to support in good faith the majority’s reasoning, may feel cornered and compelled to express not only disagreement with the majority’s final decision, but the rationale for the dissenting vote.

To conclude, in a real world with an ample supply of “hard cases” –otherwise the parties would not have gone to arbitration- and a limited availability of Herculean arbitrators –Jan Paulsson being probably among them-, doing away with party-appointments would probably be a bad idea which, in investment arbitration, might likely lead down the road to its logical conclusion: the establishment of a Permanent Multilateral Investment Tribunal, as the one envisaged in article 8.2 of the EU-Canada CETA Treaty.

But it is true that being a good party-appointed arbitrator requires effort and a knack for balancing fairness and impartiality with rigour and strength in defending your views and playing the “ombudsperson” role. For some, like Mr. Klock, this balancing act may feel as an unbearable “ethical burden”. But Truman’s famous political *dictum* might apply here:

“If you can’t stand the heat, get out of the kitchen”.