Challenge of the Arbitrator on the Grounds of Nationality: Shift in the ICAC Approach Needed

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International arbitration is based on the fundamental idea of independence and impartiality of the arbitrators settling disputes between companies originating from different states in a neutral forum. For this purpose, the parties are free to appoint arbitrators among specialists of any nationality (of course, subject to the requirement of proficiency in a language of arbitral proceedings). At the same time, arbitrators are expected to be free from any conflict of interests and remain independent of the parties, their counsels and not be reasonably engaged in the dispute in any way beyond their role as arbitrators.

If there are reasonable doubts as to the independence or impartiality of an arbitrator, a special procedural tool of challenging such an arbitrator is available to a party concerned. Under Article 12 (2) of the *UNCITRAL Model Law on International Commercial Arbitration* (which is virtually verbatim is reproduced in Article 30 (1) of the Rules of the International Commercial Arbitration Court (ICAC) of the Ukrainian Chamber of Commerce and Industry (UCCI)), a party may challenge an arbitrator, *inter alia*, if circumstances exist that give rise to justifiable doubts as to the arbitrator's impartiality or independence. Typically, arbitrators are challenged on the grounds of a conflict of interests, either personal or professional; such grounds are listed in formally non-binding but nevertheless very persuasive and internationally respected IBA Guidelines on Conflicts of Interest in International Arbitration (2004). Notably, the IBA Guidelines are silent as to nationality of an arbitrator as a ground of his/her challenge.

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Under the general rule (reflected, in particular, in Article 11 (1) of the UNCITRAL Model Law), no person shall be precluded by reason of his nationality from acting as an arbitrator, unless otherwise agreed by the parties. Generally respecting the right of the parties to appoint arbitrators with any nationality as well all the right of the party-appointed arbitrators to appoint a presiding arbitrator of any nationality, the UNCITRAL Model Law nevertheless recommends that in cases, when the parties failed to agree on the candidature of a sole arbitrator, or the party-appointed arbitrators failed to agree on the candidature of the presiding arbitrator, such a candidature is to be appointed by the "court or other authority", with due account to be given to "the advisability of appointing an arbitrator of a nationality other than those of the parties" (Article 11 (5).

At the same time, rules of arbitration courts around the world often adopt a far stricter approach on the requirement of a neutral nationality of an arbitrator. For instance, according to Article 6 (1) of the LCIA Arbitration Rules, where the parties are of different nationalities, a sole arbitrator or chairman of the Arbitral Tribunal shall not have the same nationality as any party unless the parties who are not of the same nationality as the proposed appointee all agree in writing otherwise. A very similar mandatory requirement of neutrality of the arbitrator's nationality can be found in the Rules of the International Court of Arbitration of the International Chamber of Commerce (Article 13 (5)) or in the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (Article 13 (5) and (6)).

The Ukrainian ICAC Rules, closely following the UNCITRAL Model Law, entrust the UCCI President with the function of appointing an arbitrator in the absence of an agreement of the parties or the party-appointed arbitrators, subject to "advisability" of a neutral nationality of an appointee (see Articles 27, 28 of the ICAC Rules). In practice, the ICAC refuses to treat the general advice of neutrality of the arbitrator's nationality as mandatory in nature or binding in any way upon the UCCI President; as a result, challenges on this ground of the arbitrator's nationality are invariably dismissed due the lack of any legal obligation in this respect.

At the same time, specific circumstances of a particular dispute are sometimes capable of upgrading a general advisability to something definitely more imperative than a mere recommendation, thus giving rise to a legitimate expectation of a party that the arbitrator's nationality criteria is treated in this particular case with much greater care.

As a matter of practice, nationality concerns most often arise when an international dispute handled by the ICAC involves a Ukrainian state enterprise as a respondent.

Importantly, nationality is not just a passport in someone's pocket, but a legal relationship of an individual to, or legal association with, the state. In Ukraine, nationality usually means a place of residence and the center of vital interests.

Additionally, it is problematic to detach the state enterprise from

the state which (through the government) exercises full control over the enterprise and frequently finances it. For this reason, for instance, the European Court of Human Rights (ECHR) has repeatedly affirmed (including cases involving Ukraine — see, e.g., State Holding Company *Luganksvugillya v. Ukraine* (dec.) No.23938/05, 27 January 2009) that state enterprises or state-owned or state-controlled companies shall be deemed "governmental organizations" having no recourse to the Convention mechanisms, in order to prevent a state acting *de facto* as both an applicant and a respondent party.

Moreover, arbitration proceedings against Ukrainian state enterprises may give rise to specific execution procedures affecting public interests. In general, arbitral awards duly recognized in Ukraine are enforced under the same procedures as court judgments. However, as a matter of practice Ukrainian state enterprises are frequently undercapitalized and under-financed having no funds to comply with the award, while their fixed assets (often the only valuable property they own) are immune from foreclosure due to the still effective 2001 "temporary" moratorium. At the same time, pursuant to the *On the State Guarantees of Execution of the Court Decisions Act of Ukraine of 5 June 2012, No. 4901-VI* (which was adopted in response to the ECHR case law which had consistently found Ukraine in breach of its obligations under the Convention through systematic failure to enforce final court decisions), if the monetary court decision against a state enterprise is not enforceable due to a lack of funds, the claim is to be re-directed to the State Treasury and paid from the state budget. That is, ultimately, from the pockets of Ukrainian taxpayers.

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Last but not least, as disputes involving state enterprises normally arise out of public procurement contracts, in Ukrainian realities such disputes are often marred with scandalous circumstances, allegations of corruption or embezzlement of public funds, which attracts increased attention from the media, leading to negative coverage and extensive public discussions and are accompanied by pending criminal investigations.

All the above circumstances, especially if they exist in unison, are capable of casting a justifiable doubt on the impartiality and the lack of pre-judgment of arbitral tribunal which is predominantly of Ukrainian nationality. (Needless to say, it is absolutely unacceptable when a sole arbitrator or majority of arbitrators in a dispute against the respondent state enterprise is (are) not only Ukrainian nationals but also civil servants — which is possible taking into account the ICAC list of recommended arbitrators.)

Thus, although the ICAC Rules mention only a general advisability of the neutral nationality of an arbitrator (arguably unenforceable as such), and only in cases of the UCCI President appointments, in disputes with an obvious and significant public element (a state enterprise or a government-controlled company as a respondent, broad negative media coverage, etc.) the appointment of a sole Ukrainian arbitrator or majority of the Ukrainian arbitrators in the panel, unless expressly agreed by the parties, shall be avoided to the extent possible; any such appointment shall be presumed to give rise to a reasonable doubt as to impartiality of the tribunal and, accordingly, be challengeable by a foreign claimant.

Ignoring the issue of a neutral nationality of an arbitrator in the "obvious public element" cases, beyond being capable of compromising the tribunal's international reputation, may potentially also hinder enforcement of an award rendered by such tribunal, especially in jurisdictions treating the neutrality of the arbitrator's nationalities much more seriously.

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