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ADVERSE INFERENCES DRAWN IN INTERNATIONAL ARBITRATION UNDER THE PRAGUE RULES

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ABSTRACT

International arbitration is the widely preferred method of resolution for cross-border disputes. However, it is subject to criticism for its increasing costs and length along with inefficiencies to its users who attribute these characteristics to the lack of effective sanctions available during the process. To reflect upon this dissatisfaction, new rules on the efficient conduct of arbitration were signed at the end of 2018, referred to as the Prague Rules. The Prague Rules grant arbitrators a broad power to draw adverse inference with regard to a party's case or position, if the party refuses to comply with the arbitrators' order or instruction. This possibility is not new to international arbitration. However, to date, arbitrators were reluctant to draw adverse inferences and, if they used such power, it was for reasons of evidence gathering rather than of effective case management. The Prague Rules encourage arbitrators to employ this discretion more broadly to nudge recalcitrant parties to abstain from dilatory practices and to conduct themselves in good faith.

Keywords: *The Prague Rules, adverse inference, rule of evidence, burden of proof, sanctioning powers, efficient conduct of arbitration*

1. Introduction

Arbitration is a contractual party-driven mechanism that is the favoured method of dispute resolution and applied in majority of international transactions and transnational projects. This alternative to litigation is preferred by in-house counsels and private practitioners by a margin of over 90 per cent as the option for resolving cross-border disputes both as a stand-alone mechanism and also

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together with mediation or other alternative processes.³ The preference of the arbitral process over national courts was generally attributed to its (actual or supposed) greater effectiveness, speed, expertise, confidentiality, lower costs and strong emphasis on the principle of autonomy of the parties, leaving the parties with leeway to tailor the proceedings to fit their needs and the particularities of the dispute.⁴ However, these attractive features of international arbitration have become subject to wide criticism as the international community argues that the mechanism is no longer as efficient as it was originally designed to be.⁵

This shift in the perception of international arbitration was manifested by various international surveys assessing the upsides and downsides of instruments used for dispute resolution. Where international arbitration was concerned, the majority of respondents selected the option of enforceability of arbitral awards as the most valuable characteristic of international arbitration, with avoiding specific legal systems or national courts coming second. Furthermore, users of international arbitration were also asked to indicate what they are most discontent with. By a significant margin, “cost” was voted to be the worst characteristic of arbitration, followed by the “lack of effective sanctions during the arbitral process”. The results confirmed the prevalent perception of international arbitration as ultimately the worst characteristics of international arbitration have remained unchanged for several years.⁶

³ Queen Mary University of London, *2018 International Arbitration Survey: The Evolution of International Arbitration*, London, 2018, <<http://www.arbitration.qmul.ac.uk/research/2018/>>, last accessed on 24 June 2019.

⁴ See also I.A. Council of Europe, Venice Commission, *Can Excessive Length of Proceedings be Remedied?*, 2007, 44 Science and Technique of Democracy; *Sümerli v Germany* (2006) ECHR Case No. 75.529/01.

⁵ P. Rees QC, *Arbitration – Elastic or Arthritic?*, 2017, 19 Asian Dispute Review 3, pp.104-111; K. P. Berger, J. O. Jensen, *Due process paranoia and the procedural judgment rule: a safe harbour for procedural management decisions by international arbitrators*, (2016) 32 *Arbitration International* 3, pp. 415-435; M. McIlwrath, R. Schroeder, *The View from an International Arbitration Customer: In Dire Need of Early Resolution* (2008) 74 *Arb* 3, 6-7; K. P. Berger, J. O. Jensen, *It Takes Pressure to Form Diamonds: The Changing Landscape of Dispute Resolution and Its Implications for International Arbitration*, <<http://arbitrationblog.kluwerarbitration.com/2016/05/23/the-changing-landscape-of-dispute-resolution-and-its-implications-for-international-arbitration/>> last accessed on 24 June 2019.

⁶ Queen Mary University of London Survey 2018 (footnote 3); Queen Mary University of London, *2015 Improvements and Innovations in International Arbitration* (London, 2015), <<http://www.arbitration.qmul.ac.uk/research/2015/>> last accessed on 24 June 2019; Queen Mary University of London, *2013 Corporate Choices in International Arbitration: Industry Perspectives*, (London, 2013), <<http://www.arbitration.qmul.ac.uk/research/2013/#d.en.493207>> last accessed on 24 June 2019; Queen Mary University of London, *2008 Corporate Attitudes: Recognition and Enforcement of Foreign Awards* (London, 2008), <<http://www.arbitration.qmul.ac.uk/research/2008/#d.en.493188>> last accessed on 24 June 2019; Queen Mary University of London, *International arbitration: Corporate attitudes and practices 2006* (London, 2006), <<http://www.arbitration.qmul.ac.uk/research/2006/#d.en.493194>> last accessed on 24 June 2019.

One of the reasons causing inefficiency in international arbitration is the so-called ‘due process paranoia’. This is understood as a reluctance or aversion of arbitrators to decisively use their powers for fear of the final award being challenged and set aside on the basis of the denial of the parties’ opportunity to present their respective cases fully.⁷ This phenomenon has gained attention among dispute resolution practitioners because it has led to arbitrators granting unreasonable procedural requests from parties that were effectively dilatory practices. If the proceedings become indeterminably delayed by unsolicited briefs due to a lack of effective sanctioning powers of the arbitrators or their reluctance to use them, the costs and length of the process may significantly increase.⁸ The international community thus applauds arbitrators who refuse to “allow the arbitration to be turned into a ‘circus.’”⁹

As the due process paranoia and arbitral inefficiencies became major sources of concern, many arbitration institutions started to address this in their respective rules on arbitral procedure, guidance notes, best practice sets and other soft law documents. One of the newest instruments are the Rules on the Efficient Conduct of Proceedings in International Arbitration which were signed on 14 December 2018 in Prague for which they are commonly referred to as the Prague Rules (the “**Prague Rules**”).¹⁰

The Prague Rules represent a set of rules that give arbitrators more control over the process whilst also encouraging them to use their discretion to avoid due process paranoia. The Prague Rules grant more investigative and managerial powers to arbitrators so that they can conduct the process in a more effective manner. In line with these streamlining aspirations, the Prague Rules also grant arbitrators sanctioning authority.

This article focuses on the notion of adverse inferences that is usually contained within an arbitrator’s sanctioning authority, although it stands as an evidentiary remedy rather than a threat. For this reason, the general sanctioning powers of arbitrators will be discussed first (*part 2*). Subsequently, the notion of adverse inference will be analysed from the perspective of current arbitration practice (*part 3*) and then distinguished as a concept implemented into the Prague Rules (*part 4*). Final remarks will be in the conclusion (*part 5*).

⁷ Queen Mary University of London Survey 2018 (footnote 3), Queen Mary University of London Survey 2015 (footnote 6).

⁸ K. P. Berger, J. O. Jensen, *Due process paranoia and the procedural judgment rule: a safe harbour for procedural management decisions by international arbitrators*, (2016) 32 *Arbitration International* 3, pp. 415-435.

⁹ *On Call Internet Services Ltd v Telus Communications Co* [2013] BCAA 366, [18]; see also *Triulzi Cesare SRL v XinyiGroup (Glass) Co Ltd* [2014] SGHC 220, [151] citing H. M. Holtzmann, J. E Neuhaus, *A Guide to the UNCITRAL Model Law on International Commercial Arbitration: Legislative History and Commentary*, Kluwer, 1989, p. 551.

¹⁰ Rules on the Efficient Conduct of Proceedings in International Arbitration 2018, <https://www.pragerules.com/prague_rules/>, last accessed on 24 June 2019.

2. Sanction powers of arbitrators

International arbitration gives parties the flexibility to agree on, or depart from, most procedural arrangements. However, when disputes arise, it may not be feasible for parties to come to such an agreement as their interests may be in conflict. In such cases, it is the arbitrator's task to determine the procedure, set a timetable for the filing of parties' submissions or requests, limit the number of written motions and define the manner of communication and providing evidence.

Nonetheless, in practice, there may be a difference between the notion of arbitrators' authority and the willingness of parties to comply with the authority. This gap gave rise to controversy surrounding taking of evidence and the parties' obligation to discharge their respective legal burdens of proof. As a general rule applicable in international arbitration, the burden of proving a claim remains with the party making the claim. Thus, each party must present evidence that proves that the claims and assertions it relies upon actually occurred. There is no exhaustive list of specific pieces of evidence that a party is mandated to present so as to substantiate its position and, accordingly, the parties will try to discharge the burden of proof by any piece of evidence that is in support of its case. In this sense, having access to the right documents and information may be decisive for the party's chance of success.

Nonetheless, a party often finds that it is missing a key piece of evidence. If the party reasonably believes that the other party has the missing evidence in its possession, it may request the arbitrator to order the other party to disclose it. However, in such situations, the requested document would probably contain information harmful to the other party's case and, quite naturally, the party may be unwilling to provide it to the tribunal. Thus, if the party fails to provide the requested document or fails to present a witness testimony, be it either due to the document's genuine absence or the party's reluctance, the pressing question is how the tribunal decides a case where crucial evidence is lacking.

In this sense, it must be noted that arbitral tribunals, as entities deriving their existence from private law and the agreement of the parties, by definition, lack the *jure imperii* force of national courts and are limited in their coercive powers.¹¹ They cannot enforce arbitral orders as the courts can by charging for contempt or requesting police assistance. To the contrary, arbitrators must often rely either on active participation of the parties during the process, or on authoritative instruments of state power ensuring that an order issued in arbitral proceedings is complied with. Such a situation may be illustrated by the US Federal Arbitration Act that authorizes arbitrators to summon witnesses. If a witness refuses to obey the order or is otherwise absent or neglectful, a US district court can force the

¹¹ A. Redfern, M. Hunter, *Law and Practice of International Commercial Arbitration*, 4th ed, London, Sweet & Maxwell, 2004, p. 73.

witness to attend and punish him for contempt in the same manner as it would for a similar failure to appear before the courts of the United States. Thus, although a US arbitral tribunal is vested with the power to summon witnesses, the actual sanctioning power to induce compliance remains with US national courts.¹²

However, having to merely rely on either the good faith of the parties or concurrent national proceedings to ensure cooperation from the parties and the efficient conduct of the arbitration would not be effective. Moreover, as mentioned above, avoidance of national courts is one of the most sought after features of international arbitration, also for the confidentiality and privacy of the process which may become effectively futile after a local court's intervention.

For this reason, some national arbitration laws give arbitrators the authority to incentivize compliance of parties by using tools within the arbitral process. For example, French *lex arbitri* grants arbitrators the discretion to order a recalcitrant party to pay financial penalties for non-compliance with an arbitrator's instructions.¹³ In comparison, in the Czech Republic, this option is only available to Czech civil courts under the Czech Code of Civil Procedure, although it also proportionately applies to arbitration.¹⁴ In particular, Czech courts may fine a person that either manifestly impedes the process by failing to appear before the court, fails to comply with the court's direction or disrupts the order, regardless of whether the person is a party to the proceedings or a third party.¹⁵ For example, Czech courts may impose sanctions in situations where a party refuses to visit an expert and undergo DNA sampling.¹⁶ However, if arbitrators are to be empowered to implement any similar sanctions when acting under Czech law, they must be explicitly entrusted to do so by the parties or applicable procedural rules. Otherwise, the arbitrators are only allowed to gather evidence and hear witnesses, if this was voluntarily made available to them by the parties.¹⁷

Another generally recognized sanction is represented by an arbitrator's ability to decide on cost allocation. In international arbitration, two mutually exclusive principles apply where the costs of proceedings are concerned. First is the principle of 'costs shifting' where the successful party will be reimbursed for costs incurred in the arbitration by the losing party. The second principle mandates the parties to bear their own costs of the proceedings regardless of the outcome. However, the arbitrator may be granted discretion to allocate the costs

¹² US Code: Title 9, Chapter 1, [7].

¹³ Code de Procédure Civile (France), [1467], see also Wetboek van Burgerlijke Rechtsvordering (Netherlands, Code of Civil Procedure), [1056].

¹⁴ Act No. 216/1994 Coll., on Arbitration Proceedings and Enforcement of Arbitral Awards (Czech Republic), [30].

¹⁵ Act No. 99/1963 Coll., on Civil Procedure (Czech Republic, Code of Civil Procedure), [53, 129].

¹⁶ ÚS I. ÚS 987/07 [SR 5/2008] (Constitution Court of the Czech Republic) 168.

¹⁷ Arbitration Act (footnote 14), [20].

taking into account the behaviour of the parties during the arbitration. If a party resorts to unreasonable demands or causes improper delays to the process by its absence or lack of cooperation, arbitrators may reflect upon such conduct in their allocation of costs to disadvantage of the liable party.¹⁸

This option is also available to arbitrators under the Prague Rules which grant arbitrators the power to give regard to the parties' conduct, cooperation and assistance during the arbitration as well as their absence when deciding on allocation of costs in a final award.¹⁹ Comparatively, under the IBA Rules on the Taking of Evidence in International Arbitration (the "**IBA Rules**"), arbitrators may take into account failure of a party to conduct itself in good faith as evidence in assignment of costs of the arbitration.²⁰ Despite the fact that the instrument is identical, the scope of its application is broader under the Prague Rules as it does not only pertain to evidence, but also the actions of the parties that influence their conduct in proceedings in a cost-efficient and expeditious manner.

Thus, if the parties chose application of the Prague Rules, the power of arbitrators to allocate costs to the disadvantage of the recalcitrant party should be guaranteed. However, the Prague Rules do not expressly provide for the possibility to impose monetary penalties and the parties, if they so wish for the arbitrators to have such powers, should authorise them to do so by either choosing a *lex arbitri* allowing for this course of action or to grant them such powers specifically.

All of the above described sanctioning instruments may be used to force compliance of parties and ensure a proactive approach during arbitration due to the threat of punishment. However, they do not ease the arbitrator's task of resolving a dispute where essential evidence was not produced. In these cases, the arbitrator may respond by the drawing of adverse inference which does not stand for a mere threat inciting party's participation in the process, but may be used as a tool of evidence gathering and, under the Prague Rules, as an instrument of effective case management.

3. Adverse inferences in international arbitration practice

Adverse inference is based on the notion that parties are under the duty to arbitrate fairly and cooperate in good faith compelling them to not obstruct the

¹⁸ ICC Commission Report, *Decisions on Costs in International Arbitration* (2015) 3 ICC Dispute Resolution Bulletin 1, [7]; ICC Commission Report, *Reducing Time and Costs in International Arbitration* 2nd ed., ICC 2012.

¹⁹ Prague Rules (footnote 10), [11].

²⁰ IBA Rules on the Taking of Evidence in International Arbitration 2010, [9] <<https://www.ibanet.org/Document/Default.aspx?DocumentUid=68336C49-4106-46BF-A1C6-A8F0880444DC>> last accessed on 24 June 2019.

proceedings.²¹ In line with this understanding, a party should comply with a tribunal's request, if the requested cooperation was favourable or neutral to the party's position. Conversely, if a party fails to conduct itself in the ordered manner, arbitrators may come to the conclusion that the party instructed to provide cooperation to the tribunal did not do so because the cooperation sought was unfavourable to that party's case.²²

It follows that to draw a negative inference requires seeking to establish the intention of the party neglecting the order. This requirement would lead the arbitrators to interpret the party's conduct and once the intention is found, arbitrators may assign to the action of a party the purpose that the party attached to it. In other words, it is the party's fear to present evidence that contains unfavourable information that harms the party's position that arbitrators may consider as of indirect evidential value.²³ Based on this, the arbitrator may come to the conclusion that an unproven allegation by one party is true because the other party was incapable of proving otherwise as it rather refused compliance.²⁴ Adverse inference is not a punishment for non-compliance, but rather serves as a rule of evidence that may be assigned circumstantial value. Thus, adverse inference is a substitute for when key documents are not produced that constitutes

²¹ *Metal-Tech Ltd v Republic of Uzbekistan* (2013) ICSID Case No ARB/10/3, Award, [244]; *Libananco Holdings Co v Republic of Turkey* (2008), ICSID Case No ARB/06/8, Decision on Preliminary Issues, [78]; *Methanex Corp v United States of America* (2005) Final Award pt II, ch I – 26, [54], see also IBA Rules (footnote 20), [Preamble, 3]

²² Ch. N. Brower, *The Anatomy of Fact-Finding before International Tribunals: An Analysis and a Proposal Concerning the Evaluation of Evidence* in Lillich (ed), *Fact-Finding before International Tribunals*, 147, 151, Transnational Publishers, 1991, *Biwater Gauff Ltd v United Republic of Tanzania* (2006) ICSID Case No ARB/05/22, Procedural Order No. 2, 6, citing Ch. Schreuer, *The ICSID Convention: A Commentary*, Cambridge University Press, 2001, 656; cf *Spyridon Roussalis v Romania* (2011) ICSID Case No ARB/06/1, Award, [436]

²³ *Case of Certain Norwegian Loans*, Judgment [1957] ICJ Rep 9, [35] (Separate opinion of Sir Hersch Lauterpacht); *South-West Africa Case, Judgment* [1966] ICJ Rep 6, [430] (Dissenting opinion of Jessup, J); J. H. Wigmore, *Evidence in Trials at Common Law*, 1979, 192 Little, Brown, Chadbourn rev 2, 285

²⁴ Greenberg, F. Lautenschlager, *Adverse Inferences in International Arbitral Practice*, 2011, 22:2 ICC Arbitration Bulletin 43, where an example is given which is modelled on an actual ICC award (*not defined*) where party A purchases ten shipments of raw material from party B together with reports on their quality. A mixes first six shipments and sells the final mixture to its customers. Soon A starts receiving complaints as regards to the quality of the mixture and when A tests the raw material from the seventh shipment that remained unmixed with other materials, it found the seventh shipment was of significantly inferior quality that was agreed with B. In the dispute, there is evidence that B might have conspired with a laboratory to forge reports regarding the quality of the raw material. When ordered by the arbitrators, B refuses to present documents underlying the reports and materials enlightening the origin of the raw material. Based on this non-compliance, the arbitral tribunal drew adverse inference that all ten shipments were below the required quality standard, although A had no evidence that the first six (already mixed and sold) shipments were of inferior quality.

“a genuine piece of evidence that fills a gap in a case otherwise incapable of being proven.”²⁵

The majority of jurisdictions allow, to some extent, the use of inferences as indirect evidence where a party is unable to furnish direct proof of facts or breaches of law that gave rise to liability of the other party.²⁶ The general concept is also not foreign to international arbitration.²⁷ There is constant jurisprudence confirming the inherent authority of arbitrators to draw adverse inferences from a party’s unjustified failure to cooperate.²⁸ This inherent authority is based on the broad power of arbitrators to admit and assess evidence and to manage the process for which the failure to comply (or imperfect compliance) with an arbitrator’s order gives rise to adverse inference and is usually linked to the production of requested information or documents. Thus, for instance, the IBA Rules link the possibility to draw adverse inference to the failure of a party to provide a requested document or to make available any other relevant evidence, including testimony, without a satisfactory explanation.²⁹

However, adverse inference is circumstantial evidence that, alone, may raise a suspicion that tips the scale of probabilities rather than constituting a reasonable conviction. This negative assumption may lead to the conclusion that a party is liable only together with other information, evidence or the party’s behaviour pointing towards such a conclusion. Despite its evidentiary gap-filling value, no party should be allowed to win a case relying merely on adverse inference. Preferably, the party asserting a position should always present evidence that would make its case look at least plausible.³⁰

²⁵ *Idem*

²⁶ See Code De Commerce, [L110-3] (France); Zivilprozessordnung, [286] (Germany); Grazhdanskii Protsessual’nyi Kodeks Rossiiskoi Federatsii, [55] (Russia);Codigo Procesal Civil y Comercial de la Nacion, [378, 386] (Argentina).

²⁷ M. J. Solis, *Adverse inferences in investor–state arbitration* 201834 Arbitration International 1, 79–103; S. Greenberg (footnote 22); J. K. Sharpe, *Drawing Adverse Inferences from Non-Production of Evidence*, 2006, 22 Arbitration International 549; *Corfu Channel Case*, Judgment [1949] ICJ Rep 4, 18.

²⁸ *Libananco* (footnote 21), [78]; *Central Front – Eritrea’s Claims* 2, 4, 6, 7, 8, & 22, Eritrea-Ethiopia Claims Commission, 16 RIAA 115, 131, Partial Award, [71]; *William J Levitt v Islamic Republic of Iran* (1991), Award No 520-210-3, 27 Iran-US Cl Trib Rep 145, 163, [61]; *Rumeli Telekom AS v Republic of Kazakhstan* (2008) ICSID Case No ARB/05/16, Award, [444].

²⁹ IBA Rules (footnote 20), [9/5,6].

³⁰ *R v Exall* (1866) 4 F & F [922, 929]; Greenberg (footnote 24), V. van Houtte, *Adverse Inferences in International Arbitration*, in T. Giovannini, A. Mourre, eds., *Written Evidence and Discovery in International Arbitration: New Issues and Tendencies*, Dossier VI, ICC Institute of World Business Law, Paris, ICC, 2009, p. 205.

4. Adverse inference under the Prague Rules

Adverse inferences are generally recognized as an evidential consequence of a party's failure to bring requested documents or witnesses before an arbitrator which indicates that the party feared to do so. However, there may be also other procedural orders of arbitrators that aim to ensure an efficient process. In managing arbitration, the tribunal may order, or accept a request to order, a party to comply with its instructions. Article 10 of the Prague Rules gives a tribunal the power to draw adverse inference, where it considers it appropriate with regard to a party's case or issue, if the party does not comply with the tribunal's order or instruction without justifiable grounds.

Accordingly, under the Prague Rules, adverse inference could be drawn also as a consequence of a party's failure to provide experts with requested information or with access to the subject matter of the expert examination, or if it otherwise obstructs the proceedings³¹. It is not limited to the provision of evidence but it is still based on the notion of party's obligation to act fairly. The rationale behind the broader concept of adverse inference is that dilatory practices may also amount to attempts to conceal the truth for which the evidentiary purpose of adverse inference is applicable.

It follows that the concept of adverse inference implemented into the Prague Rules serves two purposes. Firstly, it is a truth-seeking instrument for (indirect and circumstantial) evidence gathering to apply where a party fails to provide requested documents, information or testimonies. Secondly, it is also a tool of process management based on the parties' obligation of good faith participation in arbitration, generally inciting parties to refrain from unreasonable or unresponsive behaviour, thus making the arbitration procedurally more effective. In both instances, adverse inference may help the arbitrators to decide a case even though a party refuses to cooperate, is neglectful or absent.

In order to draw adverse inference, several conditions must be fulfilled. Article 10 of the Prague Rules provides that the arbitral tribunal may draw an adverse inference with regard to such party's respective case or issue only if a party does not comply with the arbitral tribunal's order(s) or instruction(s) (*part 4.1.*), without justifiable grounds (*part 4.2.*), and the arbitrators consider it appropriate (*part 4.3.*), giving them the discretion to decide in each case whether to draw the adverse inference or not. Nonetheless, the Prague Rules do not specify the extent to which the criteria must be fulfilled. To conduct such an analysis, it is convenient to turn to the international arbitration practice for guidance.

³¹ For example by arbitrary repeated requests for adjournment of a hearing.

4.1. Prior order or instruction mandating a party to provide cooperation

The concept of adverse inference implies that, firstly, there must be a prior request mandating a party to provide certain cooperation. For example, in *Methanex Corp v United States of America*, Methanex submitted that the United States failed to provide evidence (including NAFTA's negotiating history), that key witnesses were absent and that the United States blocked Methanex from gathering third-party evidence from a national court. On the basis that the United States prevented discovery, Methanex invited the arbitrators to draw adverse inferences against the United States.³² The United States contended that no adverse inferences are to be drawn because the criteria allowing for their drawing were not met. In the final award the tribunal rejected the adverse inference request principally because Methanex should have pursued an application to the tribunal to order the United States to make available the documents and testimonies if they were relevant and there were material gaps in the evidentiary record. Since Methanex did not petition the tribunal to mandate the United States to cooperate, no order was issued to that effect and, subsequently, no unjustified compliance could have been substantiated.³³ Instructing a party to provide certain cooperation is thus essential if adverse inference is to be drawn.

It also follows from the example of *Methanex v United States* that, when assessing whether to grant one party's petition to order certain cooperation to the other party, arbitrators consider if the required cooperation is relevant and important to the outcome of the case.³⁴ Thus, the party usually proposes a certain allegation that is in itself insufficient of proving a case but is nonetheless of value to the outcome of the case to the extent that arbitrators become convinced enough to order production of further documents.³⁵

Furthermore, it must not be possible for the requesting party to arrange for production of the evidence itself, which usually comes down to an analysis of whether the party has the requested piece of evidence already in its possession, within its control or it is otherwise available to it from the public domain.³⁶ Additionally, the tribunal should also ask itself whether the order is timely, sufficiently specific and whether it would be overly burdensome for the obliged party to comply with it and result in an imbalance of fairness and procedural equality between the parties.³⁷

³² *Methanex v United States* (footnote 21), pt II, ch C – 13, [23].

³³ *Methanex v United States* (footnote 21), pt II, ch G - 14–15, [25–26].

³⁴ See also Prague Rules (footnote 10), [4/4.5/a], IBA Rules (footnote 20), [3/3/b].

³⁵ Greenberg (footnote 24)

³⁶ See also Prague Rules (footnote 10), [4/4.5/b, c], IBA Rules (footnote 20), [3/3/c/i].

³⁷ See also Prague Rules (footnote 10), [4/4.3], IBA Rules (footnote 20), [3/3/a/i, ii], [3/3/c/i].

Taking into consideration all of these factors, the arbitrator should assess whether the requested cooperation is appropriate and reasonable under the specific circumstances.³⁸

4.2. Denial on justified grounds and sufficient opportunity to comply

Secondly, the tribunal must assess whether the party ordered to provide cooperation had adequate opportunity to comply with the instruction. Similarly, if a party decides to resist the order, it must be given an opportunity to justify the non-compliance.³⁹

Parties may raise various defences as to why their non-compliance with a tribunal's instruction is justified. The majority of such defences include asserting the privileged and confidential nature of the document, trade secrets and other commercial and technical reasons. Such circumstances may be due to either a legal or ethical impediment (pertaining, for example, to attorney-client privilege or individual medical records) or special political or institutional sensitivity which are recognized grounds for non-disclosure of evidence under many arbitration rules.⁴⁰ For example, the defence of secrecy was raised in the Corfu Channel case held between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the People's Republic of Albania before the International Court of Justice.⁴¹ The case concerned Albania's claim that the United Kingdom sent its warships to the Corfu Channel without approval from Albania and that passage of the warships was not innocent. The International Court of Justice ordered the United Kingdom to present materials or to disclose information that could clarify the nature of the warships' passage. However, the United Kingdom refused to comply with the disclosure order and also allowed its witnesses to refuse to answer questions relating to the materials. Instead, the United Kingdom asserted naval secrecy and presented other direct evidence contradicting Albania's allegations. Eventually, the International Court of Justice did not draw any adverse inference against the United Kingdom based on the non-compliance with the order. Apart from the naval secrecy defence, the Court took into consideration that the United Kingdom presented other evidence and

³⁸ *Azurix Corp. v. Argentine Republic* (2009) ICSID Case No. ARB/01/12, Annulment Proceeding, [209]; *Mesa Power Group, LLC v Government of Canada* (2013) UNCITRAL, PCA Case No 2012-17, Procedural Order No 5, [29]; *Peter Franz Voecklinghaus v Czech Republic* (2011) UNCITRAL, Final Award, [20].

³⁹ Solis (footnote 27).

⁴⁰ *Biwater v Tanzania* (footnote 22), 9; *Apotex Holdings Inc and Apotex Inc v United States of America* (2014) ICSID Case No ARB(AF)/12/1, Award, [8.66]; *Glamis Gold, Ltd v United States* (2005), UNCITRAL, Decision on Parties' Requests for Production of Documents; *Pope and Talbot Inc v Government of Canada* (2000), UNCITRAL, Decision by Tribunal, [1.4, 1.9].

⁴¹ *Corfu Channel Case* (footnote 27).

also gave regard to the fact that even though two UK's warships were struck by mines, the other warships did not retaliate in any way.⁴²

A party may also argue that it has no control over the requested cooperation, for example where the evidence has been lost or destroyed. Likewise, a third-party may refuse to testify as a witness or to provide certain information.⁴³ However, the event preventing the mandated party to comply with the tribunal's instruction should be shown by that party to occur to a reasonable extent.

Once the defence is presented, the analysis begins as to whether the non-compliance with the tribunal's order may be justified on the grounds presented by the obliged party. If the arbitrator finds that the proposed reasons do not justify non-compliance, they should still allow the obliged party to comply with the original instruction or allow alteration of the party's reasoning as to why its resistance is justified.⁴⁴ Denial of such a subsequent adaptation could be equal to a denial of a fair opportunity to present the party's case, as recorded in the annulment decision of the ICSID case *Fraport AG Frankfurt Airport Services Worldwide v Republic of the Philippines* where the absence of Fraport's opportunity to comment on the relevance of a document it did not provide constituted the basis for annulment of the award.⁴⁵ Similarly, the arbitrator should inform the non-compliant party of the possibility of drawing adverse inference in the award and that, possibly, the burden of producing the requested piece of evidence lies with that party, otherwise due process concerns may arise.

4.3. Adverse inference is appropriate as to its effects and relevancy

In order to establish non-compliance warranting adverse inference, there must be a prior order of the tribunal mandating a party to provide certain cooperation, the party must be provided with a sufficient opportunity to comply with the order or to present reasons for not doing so, the tribunal must find that the existing grounds do not justify the non-compliance and that the party does not subsequently provide for remedy in the form of either compliance or the presentation of different justified reasons. Only after unjustified non-compliance is established can an arbitrator begin to assess whether the drawing of the adverse inference is appropriate in the particular circumstances of the case.⁴⁶

⁴² *Corfu Channel Case* (footnote 27), 32.

⁴³ *Churchill Mining PLC and Planet Mining Pty Ltd* (2016) ICSID Case No ARB/12/14 and 12/40, Award, [251].

⁴⁴ *Biwater v Tanzania* (footnote 22), 9.

⁴⁵ *Fraport AG Frankfurt Airport Services Worldwide v Republic of the Philippines* (2010), ICSID Case No ARB/03/25, Annulment Decision, [187, 227].

⁴⁶ *Mesa Power Group, LLC v Government of Canada* (2013) UNCITRAL, PCA Case No 2012-17, Procedural Order No 5, [29]; *Peter Franz Voecklinghaus v Czech Republic* (2011) UNCITRAL, Final Award, [20].

When considering whether a specific adverse inference is appropriate, the arbitrator should first consider what effect it would have on the case at hand. As has been elaborated already, adverse inference may help circumstantially prove an alleged fact or to supplement information that is missing in the file. For example, in the ICSID case of *Europe Cement Investment & Trade SA v Republic of Turkey*, the adverse inference was drawn to demonstrate that share certificates were not produced because they would not withstand forensic scrutiny due to a lack of authenticity or because the party never owned them.⁴⁷

However, the burden of proving a claim remains with the party making the claim, even if there are evidentiary gaps in the file. Although a tribunal has broad discretion with regard to evidence assessment and evidence procedure, it cannot make an adverse inference that in effect results in modification of the legal burden of proof.⁴⁸ The arbitrator may merely shift the burden of producing specific evidence (or to provide other cooperation) onto a party that solely controls it, but the legal burden of proving a claim or defence remains unaffected.⁴⁹ Eventually, if the arbitrator remains undecided, the party alleging a position will not prevail.⁵⁰ Similarly, adverse inference alone cannot stand for conclusive evidence because of its inferior qualitative value relative to direct evidence.

It is also worth noting that discharging one party's legal burden of proof does not lead to the drawing of an adverse inference with respect to the other party's case. When one party's legal burden of proof is discharged because the other party did not provide any counter-evidence outweighing the other party's evidence, the arbitrator may make a conclusion regarding the claim in question and no inferences filling the evidentiary gaps are needed.⁵¹

Being aware of what effect the arbitrators may attribute to adverse inference, they should further assess whether it is appropriate to draw the inference with regard to the denied cooperation, factual particularities of the case, other evidence on the record and the legal burdens of the parties. In particular, the tribunal should consider whether the inference would be effective in carrying the respective claims and be sufficient to discharge the other party's burden of proof. Adverse

⁴⁷ *Europe Cement Investment & Trade SA v Republic of Turkey* (2009) ICSID Case No ARB(AF)/07/2, Award, [152, 166].

⁴⁸ Solis (footnote 27); *Asian Agricultural Products Ltd v Republic of Sri Lanka* (1990) ICSID Case No ARB/87/3, Final Award, [57]; *Metal-Tech v Uzbekistan* (footnote 21), [237]; *Limited Liability Company Amtov Ukraine* (2008), SCC Case No 080/2005, Final Award, 65.

⁴⁹ *Apotex v United States* (footnote 40), [8.8]; see also Greenberg (footnote 24) (concluding that "Adverse inferences can result in a partial shift in the burden of proof where the opposing side has provided prima facie evidence of the point it seeks to establish"); Houtte (footnote 30), 196; Sharpe (footnote 27), 551, 552.

⁵⁰ Solis (footnote 27); see also *Marvin Roy Feldman Karpa v United Mexican States* (2002) ICSID Case No ARB(AF)/99/1, Award, [177].

⁵¹ Greenberg (footnote 24), 45.

inference, as mere circumstantial evidence,⁵² sometimes does not suffice when compared with direct or a specific (expert) type of evidence that may be required for discharging the legal burden pertaining to the respective assertion.⁵³ Furthermore, adverse inference must be viewed in light of the rest of the file that may contain enough other evidence to either mitigate negative effects of the adverse inference or to negate them altogether. Moreover, in practice, there is a preference for direct evidence over indirect evidence that is of lesser probative value.⁵⁴

Accordingly, the arbitrators should consider the nexus between the adverse inference in question and the burden of proof that is necessary to carry. In other words, the essential part of the analysis lies in assessing the extent to which the arbitrators may rely on the effects of adverse inference if it is drawn. The focal point of such an assessment is the question of whether the adverse inference would be relevant to the outcome of the case. For example, in the ICSID case of *Gemplus SA et al v United Mexican States*, Mexico requested that an adverse inference be drawn based on the testimony of a witness that lied about the identity of a third party. Nonetheless, the tribunal reasoned that the identity of the third party had no relevance to the outcome of the case and thus the fact of whether the witness lied was inconsequential. Accordingly, no adverse inference was drawn.⁵⁵

The assessment of the effects of adverse inference based on its relevancy to the final award was also noted in the widely discussed case of *Achmea BV v Slovak Republic* that was held before the Permanent Arbitration Court in the award concerning the jurisdiction of the tribunal. The issue concerned a question of whether the law of the European Union was applicable and, if it was, whether its supreme application excluded application of the bilateral investment treaty on which arbitrability of the claim was based. Slovakia requested certain correspondence exchanged between Achmea and the European Commission regarding a breach of EU law by the Slovak Republic should be disclosed. However, Achmea did not provide any such correspondence. The tribunal reasoned that drawing an adverse inference would be inappropriate for dealing with the non-compliance as the tribunal was not convinced by Slovakia's argument that the applicability of EU law would disapply the respective bilateral investment treaty which would lead to stripping the arbitrators of their jurisdiction. Therefore,

⁵² *Corfu Channel Case* (footnote 27), 18.

⁵³ *OPIC Karimum Corp v Bolivarian Republic of Venezuela* (2013) ICSID Case No ARB/10/14, Award, [145, 146].

⁵⁴ *Metal-Tech v Uzbekistan* (footnote 21), [229, 265, 364]; *Glamis Gold, Ltd v United States of America* (2009) UNCITRAL, Award, [707, 822]; *Hassan Awdi et al v Romania* (2015) ICSID Case No ARB/10/13, Award, [133, 139, 201].

⁵⁵ *Gemplus SA et al v United Mexican States* (2010) ICSID Case No ARB(AF)/04/3 & ARB(AF)/04/4, Award, [4-142].

the adverse inference was not relevant to the outcome of the case, rendering it superfluous.⁵⁶

The decision as to whether to draw adverse inference from undisclosed evidence is always within the discretion of the tribunal. If the tribunal can reach settlement of the case without conducting the inference scrutiny, it does not need to resolve the question of whether the adverse inference would be appropriate to draw or what consequences it would have. Thus, when the arbitrator has a sufficient evidentiary record to prove respective claims or defences, they would often disregard the option of drawing adverse inference in support of the respective position.⁵⁷ The reason for this is that, in these cases, adverse inference would only make the prevalent party's case stronger. If the position has already been satisfactorily proven by other evidence presented by the respective party, it is not necessary to resort to adverse inference as it would not influence the outcome of the case.⁵⁸ However, if there is a lack of other evidence, drawing adverse inference may be an important tool for supplementing information. Moreover, under the Prague Rules, the arbitrators may use the possibility to draw adverse inferences as a procedural instrument of effective case management, where the above described criteria would apply to a reasonable extent.

5. Conclusion

The notion of adverse inference is generally recognized in international arbitration and is established under most arbitral procedural rules and guidelines along with support from consistent jurisprudence. Nonetheless, in practice, arbitrators were hesitant to apply their discretion to draw adverse inference, either for the fear of disruption of fair process or the inferior effects of the adverse inference in relation to other evidence filed on the record. The overall spirit of the Prague Rules encourages arbitrators to use their powers more effectively to reflect on the current grievances of users of international arbitration, among which is also a lack of sanctions. Even though adverse inference is considered a remedial rule of evidence rather than a punishment of unreasonable behaviour, the Prague Rules implement the concept to give arbitrators a tool of effective time and cost management at arbitral proceedings. While tribunals acting under

⁵⁶ *Achmea BV v Slovak Republic* (2010) UNCITRAL, PCA Case No 2008-13, Award on Jurisdiction, Arbitrability and Suspension, [19, 132-134, 140, 265, 277].

⁵⁷ Greenberg (footnote 24), 49, informs that out of 36 instances where ICC awards dealt with the option of drawing adverse inference, in 20 (58 %) cases the arbitral tribunal concluded that adverse inference was not necessary for it to reach a decision, in 12 out of 36 cases the arbitral tribunal drew adverse inference (always based on non-production of ordered documents) and in 7 cases the inference was decisive for the outcome of the case.

⁵⁸ Solis (footnote 27); Greenberg (footnote 24); *Rumeli v Kazakhstan* (footnote 28).

the Prague Rules may also be most incentivised to use this power with regard to the disclosure of evidence, they may also nudge recalcitrant parties to comply with other instructions of the arbitrators concerning the efficiency of the process. Given all conditions are met to the required extent and the arbitrator provides sufficient reasoning justifying a negative conclusion regarding a party's case or position, adverse inference may serve as a general process-enhancing instrument and arbitrators may consider it more often.

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