JUDGMENT : HHJ Anthony Thornton. TCC. 5th December 2001

1. Introduction

1. This is an appeal from an arbitrator's costs award made in a construction arbitration. The applicant is Fence Gate Limited ("FGL") who was the building employer and the respondent is NEL Construction Limited ("NEL") who was the building contractor. These parties entered into a contract in the JCT IFC 84 standard form of contract dated 2 February 1998 for the extension of, and alterations to, the dining and kitchen facilities at FGL's premises at the Fence Gate Inn, Wheatley Lane Road, Burnley, Lancashire. The resulting dispute was referred to arbitration pursuant to the arbitration agreement in the contract and, by the agreement of the parties, Mr Keith Rawson ARIBA, FCIArb, MAE was appointed as arbitrator. He accepted his appointment on 25 March 1999. A lengthy hearing was held in Burnley in March and April 2000. The arbitrator has published 5 awards. The principal award, which was award no. 2, dealt with FGL's counterclaim, save for a claim for loss of profit which had been held over for a subsequent hearing. Awards nos 1 and 4 were consent awards which incorporated agreements reached by the parties compromising, respectively, NEL's claim and FGL's loss of profit counterclaim. Award no. 3 dismissed an application by each party to correct award no. 2 and award no. 5, with which this appeal is concerned, dealt with the costs of both the claim and the counterclaim.

2. Leave to appeal pursuant to section 69(2)(b) of the Arbitration Act 1996 ("the Act") was not required. This was because the parties, by their arbitration agreement contained in clause 9.5 of JCT IFC 84, had agreed and consented to either party being able to appeal any question of law arising out of any award resulting from that agreement. It has already been decided, by Clarke J., in ***Taylor Woodrow Civil Engineering Ltd v Hutchinson Development Ltd***,[1] in relation to the same arbitration agreement, that the effect of clause 9.5 is to constitute an agreement covered by section 69(2) (a) of the Act and is, therefore, one which allows the parties to appeal any question of law arising out of an award without the need to obtain leave to appeal from the High Court. It follows that the appeal is a rarity being one involving a consideration of the powers of an arbitrator to award costs. In most cases, a question of law arising out of a costs award can only be brought with leave which, given the statutory limitations usually applying to such appeals, is rarely forthcoming.

3. The relevant award was published on 14 February 2001 and is unusually lengthy for a costs award given that it runs to 74 paragraphs and 13 pages. The reason for its length was because the arbitrator directed that there would be no oral costs hearing and the preceding written submissions were lengthy and diffuse and also because the costs award was unusual and had significant financial consequences to the parties. The award was concerned with the costs of both parties which, 4 months before the 13-day hearing, had been estimated to exceed £180,000 in an arbitration concerned with a relatively straightforward building dispute. NEL's claim had been settled prior to the hearing on terms that the costs would be determined by the arbitrator. In the costs award, the arbitrator awarded NEL its costs of the claim, to be assessed if not agreed. The hearing had only been concerned with FGL's counterclaim and, despite there having been an award on the counterclaim in FGL's favour, the costs award provided that each side should pay its own costs of that counterclaim.

4. The compromise of NEL's claim for the unpaid balance of the value of its work was for £22,000 inclusive of VAT and interest in relation to a claim totalling £32,411.82 inclusive of VAT but exclusive of interest. This agreed sum compromised not only the totality of NEL's claim but also 6 items of FGL's counterclaim which had been originally claimed by FGL in the total sum of £20,625. The combined effects of awards nos 2, 3 and 4 had been to award FGL £47,788.39 on its counterclaim inclusive of VAT and interest against a total sum claimed of about £290,000 inclusive of VAT but exclusive of interest over a period of 15 months.

5. Thus, FGL recovered a relatively small part of its counterclaim whereas NEL recovered the greater part of its claim.

2. The Arbitration

6. It is accepted practice that a court considering an appeal arising out of an award should confine its consideration to the terms of the award and its accompanying reasons and to any document incorporated into the award. The costs award was worded in a way which effectively incorporated within it the parties' written submissions, the arbitrator's earlier awards and the pleadings since the costs award was only intelligible if read in conjunction with these documents. In addition, the parties' submissions and the costs award both referred to and relied on several settlement offers made during the reference. I was therefore provided with copies of all these documents from which I have extracted the relevant background facts.

7. FGL runs the Fence Gate Inn, a listed public house in Burnley. In 1997, FGL's Managing Director, Mr Kevin Berkins, sought to implement a scheme to instal a new kitchen and brasserie to enable superior quality restaurant food and wine to be served at the Inn. Designs were prepared by Mr Andrew Little and, following a tender submitted in August 1997, NEL contracted to undertake the work. Although the date for completion was 26 April 1998, the work was programmed to be completed by 9 April 1998 and the kitchen was in fact occupied on 15 April 1998. The arbitrator found that practical completion of the kitchen occurred on 15 April 1998 and of the brasserie on 29 May 1998. Since the delay in completing the work in the brasserie was found to be the responsibility of FGL, the arbitrator also found that NEL had no liability for liquidated damages.

8. Although Mr Berkins maintained throughout the arbitration that he had appointed Mr Little as Contract Administrator, the arbitrator found that Mr Berkins took on that role from Mr Little although subsequently he

[1] [1999] ADLRJ 83.

appointed James R Knowles Limited ("JRK"), a firm of quantity surveyors and claims consultants, to this role in early July 1998. This appointment followed the preparation by JRK of a schedule of allegedly outstanding defects in NEL's work which it completed in June 1998. NEL subsequently carried out certain remedial works to the roof structure. In addition, extensive negotiations took place between JRK and NEL as to the scope and extent of the remedial works required to the kitchen but these matters could not be agreed and NEL's contract was ultimately determined by JRK and other contractors undertook the remedial works. Completion was never certified.

9. The arbitration was started by NEL with a notice of arbitration dated 30 September 1998. NEL was claiming the unpaid balance of the contract sum which included a sum for variations which NEL had valued at £20,958.47. NEL's claim was disputed in part by FGL but, essentially, was met with a set-off and counterclaim which greatly exceeded it. The principal claims included in the counterclaim related to the quality of the kitchen and brasserie floors, remedial work to these floors, the dates by which they had achieved practical completion and the loss of profit that FGL claimed it had incurred as a result of the alleged delays in completion and the defects left by NEL. The claim for the defects, as remedied by others, totalled £59,423 and the professional fees of JRK that were also claimed totalled £45,370, both sums being inclusive of VAT. The loss of profit claim was claimed in the round at an estimated sum of £100,000. No further particulars of this loss of profit counterclaim were provided when the counterclaim was first pleaded.

10. In a comprehensive first order for directions made on 23 February 1999, the arbitrator provisionally fixed the week commencing 26 July 1999 for the hearing. The order also provided a detailed timetable for pleadings, discovery and the service of witness and expert evidence. The experts were directed to meet by 8 June 1999 and then exchange reports by 15 June 1999. Once the pleadings and FGL's scott schedule and NEL's replies had been served, it became clear that the parties would not be ready for the hearing and the arbitrator re-fixed it to start on 22 November 1999 for a period of one week. In September 1999, FGL obtained an accountant's report which, for the first time, quantified its loss of profit claim. This report was dated 10 September 1999. It was subsequently served on NEL along with FGL's witness statements and its other expert's report from a building surveyor. However, no application to amend the counterclaim to plead the details or figures contained in the accountant's report was made until a much later stage and NEL did nothing at that stage to obtain or serve on FGL its own accountancy evidence despite the arbitrator's original order that all expert evidence should be exchanged by 15 June 1999.

11. In early November 1999, the parties engaged in an unsuccessful mediation. Following that, in the week before the intended hearing, both parties' respective counsel wrote a joint letter to the arbitrator seeking an adjournment of the hearing on the grounds that 5 days would be insufficient, given the large amount of documentation and evidence and the large number of disputed issues to be resolved. They estimated that three weeks of hearing time would be needed and both counsel stated that it was neither practicable nor desirable to split up the hearing or to hive off issues. The arbitrator wrote back suggesting that costs might be saved if, initially, three of what he regarded as the principle liability issues were heard and resolved in the week set aside for the hearing. However, both counsel jointly replied stating that the parties agreed that to truncate or split the hearing would be contrary to their wishes and a potential injustice. In consequence, the arbitrator agreed to adjourn the hearing and refixed it for an estimated 13-day period starting on 29 March 2000.

12. Significantly, soon afterwards, following a suggestion made by the arbitrator, the parties agreed to the loss of profit claim being hived off for hearing once the award on all other counterclaim issues had been issued. In consequence, a consent order was made on 22 December 1999 whereby the time for NEL's expert accountant to respond to FGL's accountant's report was extended until 3 July 2000 to be followed by a meeting and joint statement. A second hearing to deal with the loss of profit claim was provisionally fixed for a period in the hearing window August - September 2000.

13. On 8 March 2000, in the period leading up to the hearing, the parties compromised the claim and 6 small items of the counterclaim and this was given effect to in award no. 1 published on 26 April 2000. On the second day of the hearing, on 30 March 2000, the arbitrator made a number of procedural directions including one giving FGL leave to amend its counterclaim to plead a new schedule of loss. These amendments included the quantification of two alternative loss of profit claims that had been put forward for the first time by FGL's accountant in the report served in October 1999. These claims were based on two different periods of alleged disruption and were for, respectively, £100,900 and £171,500. Previously, the pleadings had merely claimed a figure of £100,000 with no more particularisation than: "Loss of profit estimated at £100,000". The amendment to particularise the loss of profit claim did not affect the earlier decision that all preparations for the hearing of the counterclaim for loss of profit would await publication of the award on all other counterclaim issues.

14. Following the conclusion of what turned out to be a 12-day hearing on 13 April 2000, the arbitrator published his award on 8 June 2000. The award determined 5 general issues of fact and a large number of further factual issues affecting liability set out in the detailed scott schedule and, in the light of these findings, a monetary award in favour of FGL was made which totalled £36,467.11 VAT. The award made it clear that it did not cover the outstanding claim for loss of profit (if any) and it reserved awards of interest and costs. Following that award, each party applied under section 57 of the Act to the arbitrator, in NEL's case for corrections to the award and, in FGL's case, for an additional award. NEL sought corrections to the quantification which, if made, would have changed the manner of quantification with a consequent significant decrease in the sum previously awarded. FGL

sought an additional award relating to facts that it stated would permit the quantification of the loss of profit claim. In award no. 3, published on 8 September 2000, the arbitrator dismissed both applications with detailed supporting reasons.

15. No hearing of the loss of profit claim took place in the proposed hearing window of August – September 2000. Subsequently, the parties compromised this claim in the sum of £5,000 inclusive of both VAT and interest and this agreement was embodied in a consent award, no. 4, published on 19 December 2000. By agreement, this award provided that the entitlement to costs in relation to the loss of profit claim should be determined at the same time as the determination of the costs of the counterclaim.

16. The arbitrator directed that the costs hearing would be by way of a written procedure. The parties exchanged submissions and then reply submissions. These were extremely detailed and included copies of a large number of authorities and, in FGL's case, a lengthy extract concerned with costs from the report of Lord Woolf entitled: "Access to Justice – Interim Report" which had been the prelude to the introduction in 1999 of the Civil Procedure Rules used in the High Court and the county courts. This led to the arbitrator's costs award no. 5 published on 14 February 2001. FGL's arbitration application containing its appeal from this award was issued on 12 March 2001. The hearing of the appeal occupied 2 ½ hours following the service of detailed written submissions by both parties. Many of the arguments and authorities were the same as had been provided to the arbitrator. Following the handing down of my draft judgment allowing FGL's appeal, a second hearing took place which also lasted 2 ½ hours. This hearing considered the parties' further submissions on, in particular, the question of whether my conclusion that the arbitrator's finding that the exaggerated size of the counterclaim had precluded a settlement of the counterclaim was unsupported by any evidence and should not have been relied on gave rise to an appealable question of law. The hearing also considered the difficult question of whether I should order that the costs question considered by the arbitrator should be remitted for a further hearing by him or whether, instead, I should consider what variation, if any, should be made to his costs award. Having determined that I should vary the costs order myself, a third short hearing was then held to consider the parties' submissions on the question of what variation, if any, there should be and with all other procedural questions. Finally, a fourth hearing was held to consider NEL's application for leave to further appeal my decision on the questions of law raised by this appeal. I then handed down this composite judgment which deals with all these issues.

3. The Awards

17. All three relevant awards are detailed. The principal award sets out each finding of fact needed to resolve each issue and answers each issue in detail. It is carefully structured. The section 57 award carefully addresses the issues raised by each party's application. FGL's application for further findings of fact was dismissed on the ground that these findings had not been sought in the list of issues that the parties had provided to the arbitrator for determination at the hearing. NEL's application was dismissed on the basis that the arbitrator's original quantification was correct.

18. The section 57 award also dealt with a comment that the arbitrator had made to the parties after the principal award had been published and which had been referred to by FGL in its submissions. This was to the effect that it would be difficult for FGL to persuade him that it had a sustainable claim for loss of profit. The arbitrator commented that: *"I have previously expressed my concern at the wholly disproportionate costs that have been incurred to date in relation to this reference and I felt that to meet my obligations in respect of time and costs under the Arbitration Act 1996, I should place the onus on FGL to make a decision on the pursuance of this head of claim."*

    The arbitrator also acknowledged that he could not reach a conclusion about the loss of profit claim at that stage.

19. Unlike the earlier awards, the costs award is not well structured. This is understandable since the arbitrator was seeking to respond to the detailed and, as I find in this judgment, largely irrelevant submissions that he had received from both parties. Given the radical and far-reaching changes to arbitration law and practice occasioned by the Act which, in the context of a costs appeal, have not previously been the subject of judicial consideration, it was not surprising that the submissions were in this form since they were founded on the pre-Act law and practice. The award starts with his acknowledgement that: *"Whilst I am very conscious of the need to minimise cost, the costs of this Arbitration already far exceed the sums awarded and therefore the determination of costs and interest is of the utmost importance to both parties in this fiercely contested dispute. I therefore consider that it would not do justice to either side if I were to make an award without responding in some detail to the formal submissions made to me and commenting on the extensive authorities submitted in their support. I therefore propose to run through each submission setting out my reaction to the points made, also incorporating the parties' replies during the course of my analysis where relevant."*

20. The award takes each party's submissions in turn and submits both to a point by point analysis followed by a short and succinct section entitled "Summary of Reasons on Costs" which it is helpful to set verbatim since it contains the core of the arbitrator's reasoning that is challenged in this appeal. This summary is as follows:
    "By way of summary, the following are the factors which I have taken into consideration in determining my award of the liability for costs:-
    1. Costs are at my discretion provided I give my reasons.
    2. I must have good reasons for departing from the rule that costs should follow the event and I find that there are justifiable reasons in this instance.

3. CIMAR Rule 13.3 clearly states that I should deal with the costs of the claim and counterclaim separately if I do not consider that they are so interconnected that they should be dealt with together. I have not been persuaded that the two are so interconnected.
4. The claimant made a very substantial recovery on its claim which was simple in format and presentation.
5. The magnitude of the counterclaim which had a deterrent effect on an early settlement and the fact that the hearing dealt solely with the counterclaim.
6. The loss of profit and fee claims were exaggerated.
7. The claimant was unsuccessful on five major issues at the hearing and the respondent's conduct was the subject of critical comment.
8. If I were to award costs on an issue by issue basis, this would risk prolonging the dispute. ...

I HEREBY FIND, DETERMINE, AWARD AND DIRECT:-
1. That the claimant be awarded its costs of the claim and that failing agreement, these costs be taxed by me [in accordance with the authority granted me by the parties].
2. That each party should bear its own costs of the counterclaim."

4. Summary of FGL's Grounds of Appeal

20. FGL submitted that the costs award contained a number of errors of law and that it should be set aside. FGL also asked that I should substitute an appropriate costs award myself rather than remitting the award for reconsideration, with or without a direction, by the arbitrator. The errors of law contended for may be summarised as follows:

1. The arbitrator erroneously relied on two crucial findings about the counterclaim:
   (1) it was exaggerated; and
   (2) its magnitude had a deterrent effect on an early settlement of the counterclaim.

   There was no evidence for these findings which were at variance with the actual size of the counterclaim award, the existence and contents of various settlement offers made during the reference and NEL's failure to make an appropriate offer to settle the counterclaim.

2. The arbitrator failed to have regard to the offers of settlement.

3. The arbitrator should not have relied on his criticisms of FGL's conduct contained in the principal award which related to its conduct during the contract.

4. The arbitrator failed to take into account that:
   (1) the costs of the claim had been dealt with very differently by him despite NEL's lesser claim recovery compared to FGL's counterclaim recovery; and
   (2) that the vast majority of costs were incurred on the counterclaim which was all that was in issue at the hearing.

5. The arbitrator failed to apply section 61 of the Act and Rule 13.1 of the applicable arbitration rules. In particular:
   (1) He failed to find what the relevant "event" was. Such a finding was essential before his costs award could depart from the mandatory starting point that, ordinarily, the winning party of an "event" was entitled to its costs.
   (2) He gave effect to matters which were neither material nor relevant.
   (3) He erroneously took into account certain irrelevant matters and failed to take into account certain relevant matters.
   (4) No consideration was given to the possibility of making a percentage reduction in the overall amount of FGL's counterclaim costs.
   (5) He gave inadequate reasons for his conclusion that FGL should recover none of its costs on the counterclaim.

In summary, FGL contended that the costs award was not "judicially" arrived at.

5. The Arbitrator's Jurisdiction to Award Costs

21. An arbitrator's jurisdiction to award costs is dealt with in section 61 of the Act and any procedural rules affecting costs that the parties have agreed should govern the arbitration. These parties had agreed that the arbitration would be conducted in accordance with the 1998 edition of the Construction Industry Model Arbitration Rules ("CIMAR"). As a result, Rule 13 of CIMAR concerned with costs fleshed out the arbitrator's costs jurisdiction. Thus, the arbitrator derived his costs jurisdiction from the terms of the arbitration clause of the JCT IFC 84 form of contract, sections 59 and 61 of the Act and Rule 13 of CIMAR. It is helpful to set out the material parts of these provisions.

1. Clause 9 of JCT IFC 84

"*9.3 ... the Arbitrator shall, without prejudice to the generality of his powers, have power to ... ascertain and award any sum which ought to have been the subject of or included in any certificate and to open up, review and revise any certificate, opinion, decision, requirement or notice and to determine all matters in dispute which shall be submitted to him in the same manner as if no such certificate, opinion, decision, requirement or notice had been given.*

9.5 The parties hereby agree and consent pursuant to sections 1(3) (a) and 2(1) (b) of the Arbitration Act 1979 that either party

(a) may appeal to the High Court on any question of law arising out of an award made in an arbitration under this Arbitration Agreement ... and the parties agree that the High Court should have jurisdiction to determine any such question of law."

2. Sections 59 and 61 of the Act

"59 (1) References in this Part to the costs of the arbitration are to (a) the arbitrator's fees and expenses
(b) the fees and expenses of any arbitral institution concerned, and
(c) the legal or other costs of the parties.

(2) Any such reference included the costs of or incidental to any proceedings to determine the amount of the recoverable costs of the arbitration.

61 (1) The tribunal may make an award allocating the costs of the arbitration as between the parties, subject to any agreement of the parties. (2) Unless the parties otherwise agree, the tribunal shall award costs on the general principle that costs should follow the event except where it appears to the tribunal that in the circumstances this is not appropriate in relation to the whole or part of the costs.

63 (1) The parties are free to agree what costs of the arbitration are recoverable.

(2) if or to the extent there is no agreement, the following provisions apply.

(3) The tribunal may determine by award the recoverable costs of the arbitration on such basis as it thinks fit. If it does so, it shall specify
(a) the basis on which it has acted, and
(b) the items of recoverable costs and the amount referable to each. ...

(5) Unless the tribunal or court determines otherwise
(a) the recoverable costs of the arbitration shall be determined on the basis that there shall be allowed a reasonable amount in respect of all costs reasonably incurred, and
(b) any doubt as to whether costs were reasonably incurred or were reasonable in amount shall be resolved in favour of the paying party."

3. Rule 13 of CIMAR

"RULE 13: COSTS

13.1 The general principle is that costs should be borne by the losing party: see section 61 (Award of costs). Subject to any agreement between the parties, the arbitrator has the widest discretion in awarding which party should bear what proportion of the costs of the arbitration.

13.2 In allocating costs the arbitrator shall have regard to all material circumstances, including such of the following as may be relevant:
(a) which of the claims has led to the incurring of substantial costs and whether they were successful;
(b) whether any claim which has succeeded was unreasonably exaggerated;
(c) the conduct of the party who succeeded on any claim and any concession made by the other party;
(d) the degree of success of each party.

See also Rule 13.9.

13.3 Where an award deals with both a claim and a counterclaim, the arbitrator should deal with the recovery of costs in relation to each of them separately unless he considers them to be so interconnected that they should be dealt with together. ...

13.9 In allocating costs the arbitrator shall have regard to any offer of settlement or compromise from either party, whatever its description or form. The general principle which the arbitrator should follow is that a party who recovers less overall that was offered to him in settlement or compromise should recover the costs which he would otherwise have been entitled to recover only up to the date on which it was reasonable for him to have accepted the offer, and the offeror should recover his costs thereafter."

6. The Nature of an Appeal from a Costs Award

6.1. Summary of the Law and Practice

6.1.1. Earlier Arbitration Costs Regimes

22. Costs awards and decisions of arbitrators have traditionally been difficult to challenge given the general discretion with regard to the award of costs that arbitrators have conventionally always had. There have recently been profound changes in the regime governing an arbitrator's costs powers and the judicial supervision of the exercise of those powers.

23. **Before 1979.** Before 1979, an arbitrator's powers to award costs were expressed in the most general terms, most recently in section 18 of the Arbitration Act 1950.[2] Arbitrators rarely gave reasons for their costs awards but, since arbitrators were required to decide disputes in accordance with law, the courts always considered that an arbitrator's powers to award costs had to be exercised in the same way that a judge exercised analogous costs

[2] *"Unless a contrary intention is expressed therein, every arbitration agreement shall be deemed to include a provision that the costs of the reference shall be in the discretion of the arbitrator or umpire, who may direct to and by whom and in what manner those costs or any part of them shall be paid ...".*

powers in court proceedings. An arbitrator, in consequence, had to "act judicially" which meant that he had to act in accordance with the same principles, and be subject to the same limitations, as a judge when exercising a judicial discretion to award costs. Any perceived failure to "act judicially" was regarded as constituting an excess of jurisdiction which could be challenged, but only challenged, as misconduct or, where reasons had been provided, as error on the face of the award since an arbitrator could never be required to state a case with regard to costs.

24. **Between 1979 and 1996.** The Arbitration Act 1979, which had to be applied in conjunction with the Arbitration Act 1950, abolished both the case stated procedure and judicial control of errors appearing on the face of an award and replaced these with a limited right of appeal on questions of law arising out of an award. In consequence, the only way of challenging a costs award was by way of an appeal on a question of law.[3] However, the Arbitration Acts 1950 – 1979 left unchanged an arbitrator's statutory powers with regard to an award of costs. Thus, an arbitrator's costs powers were still regarded as being analogous to those of a judge when deciding a costs question.

25. An appeal against a judicial costs decision could only have been brought if the judge who had made the relevant decision gave leave to appeal. A potential appeal usually involved challenging the discretionary exercise of the power to award costs rather than a question of law or jurisdiction. Thus, leave was rarely given. However, if a judge refused leave to appeal, it was possible to circumvent that refusal if the Court of Appeal could be persuaded that the original costs decision had been made in excess of jurisdiction. This procedure was regarded as a relevant analogy when a potential costs appeal from an arbitrator was being considered.

26. Thus, an appeal from an arbitrator's costs award involved two hurdles. Firstly, it had to raise a question of law arising out of the award and, secondly, it had to raise a similar issue to one that could be raised in the Court of Appeal when a judge had refused leave to appeal his own costs decision. It followed that leave to appeal would normally only be given from a costs award, and an arbitrator's costs appeal could only be argued, where the appeal raised a question as to whether or not the arbitrator had acted within his jurisdiction and hence judicially. The usual way of framing this question was: *"did the facts set out in the award provide grounds upon which the arbitrator could properly in law have exercised his discretion as to costs in the way he did?"* This question raised a question of law.[4]

27. **Since 1996.** The costs regime applicable to arbitrations has been radically changed by the 1996 Act once it came into force. Firstly, the Act spells out more clearly than before the express costs powers that may be exercised by arbitrators. Section 61 provides that an arbitrator may make a costs award but, in making it, the arbitrator should act on the general principle that costs should follow the event except where it appears to the arbitrator that in the circumstances this would not be appropriate in relation to the whole or part of the costs. In compliance with the general statutory principle of party autonomy,[5] section 61 also provides that an arbitrator's costs powers are to be subject to any agreement as to those powers that has previously been reached by the parties.

28. Secondly, the Act abolished judicial control of arbitrators on grounds of misconduct and has replaced it with the more limited power to intervene on grounds of serious irregularity if one of the statutorily defined grounds has been made out. For costs awards, the relevant grounds are: a failure to comply with the general statutory duties of fairness, impartiality and procedural regularity; an excess of powers; a failure to conduct the proceedings in accordance with the agreed procedure and a failure to deal with all the issues put to the arbitrator.

29. Furthermore, in 1999 the Rules of the Supreme Court were replaced by the Civil Procedure Rules.[6] The CPR contain very different and more flexible costs powers in CPR 44.3 and a different regime governing appeals from a judge's costs decision in CPR 52.3(6). Under the CPR, a potential appeal from the costs decision of a judge will usually involve a consideration of whether the judge had the power to make the relevant decision at all but, given the wide costs powers provided by Rule 44.3, this question will rarely arise in practice. Any potential appeal is no longer subject to the requirement that the judge from whom the appeal is to be brought must himself give leave or permission to appeal. Instead, a potential costs appeal may be brought with the permission of either the first instance judge or the Court of Appeal and is subject to the same requirements as to permission to appeal as any other appeal. The relevant considerations are whether the potential appeal has a real prospect of success or whether there is some other compelling reason why it should be heard.

6.1.2. The Current Costs Regime

30. An appeal arising out of a costs award may be brought: "*on a question of law arising out of an award*" (section 69(1) of the Act). An arbitrator has a **duty to provide reasons** for his award (unless the parties have agreed otherwise) and, if these have not been stated sufficiently or at all, the court can order the arbitrator to state his reasons in sufficient detail (section 70(4)). Further, a costs award may be made the subject of a challenge under section 68 of the Act on the ground of serious irregularity of a kind defined in section 68(2). As I have already

[3] See ***Blexen Ltd v G Percy Trentham Ltd*** [1990] 2 EGLR 9, (CA).

[4] See ***Everglade Maritime Inc. v Schiffahrtsgesellachaft Detlef Von Appen, The "Maria"*** [1993] Q.B. 780, (CA), per Sir Thomas Bingham M.R. at page 789; ***FKI Engineering Plc v Metro-Cammell Hong Kong Limited*** (1996) 77 BLR 84, Judge LLoyd QC sitting on Official Referees' Business.

[5] Section 1(c) of the Act which provides that the parties should be free to agree how their disputes are resolved and that the court should not intervene except as provided in Part I of the Act

[6] For a short period, between 1 February 1997 and 29 April 1999, the Act was in force alongside the RSC. The CPR then came into force. No discernibly different regime was in force in this period to that now in force with the CPR but there were no reported decisions so no firm view about this may be stated.

stated, that section includes, as one of the defined specific grounds for challenge, a complaint that the arbitrator exceeded his powers.

31. If an arbitrator has potentially exceeded his powers, the irregularity will usually be capable of being raised as a question of law. There is, therefore, when a jurisdictional question is raised, a theoretical overlap between a potential appeal on a question of law and the judicial supervision of serious irregularity. If the jurisdictional question arises out of the reasoning in the award, the appropriate potential remedy is by way of appeal since, otherwise, the statutory restrictions on appeals being brought would be circumvented. When no question of law is raised, the only potential remedy is by way of an intervention on the grounds of serious irregularity.

32. In the light of these provisions of the Act, three related questions need to be asked in relation to a costs award which a party wishes to challenge. These are:
    1. Does a question of law arise out of the award?
    2. A related but not identical question: Did the arbitrator act within his jurisdiction? If so, is the complaint one which raises a question of law?
    3. If the potential ground of challenge cannot be expressed as a question of law: Has there been any serious irregularity?

33. It is no longer helpful to ask whether an arbitrator has acted "judicially" or has acted in an equivalent way as a judge would have acted in a similar situation when reaching a judicially determined costs decision. This concept was initially developed to fill the gap provided by the perceived lacuna in the general discretion given to arbitrators when awarding costs and by the absence of an appropriate yardstick and procedure to control those powers. However, the Act has now defined an arbitrator's costs powers with precision and also provides unequivocally that the relevant provisions of the Act are founded on the principle that the court should not intervene except as provided for by Part I of the Act which should be construed accordingly.[7] In those circumstances, it is no longer appropriate to imply any gloss or further restriction onto the exercise by an arbitrator of the statutory power to award costs. This is particularly so now that the CPR have replaced the RSC since the detailed costs regime that has been introduced for the courts, although similar to that provided for by the Act, particularly when read with CIMAR, is not identical to it. Thus, it is not appropriate to refine the limited statutory basis for judicial intervention into an arbitration that the Act makes available to the court by the introduction of the concept that the arbitrator must have acted "judicially". The function of the court is to ensure that the arbitrator has acted in accordance with the express powers given to him by the Act and the parties.

34. It follows that judicial case law concerned with costs decisions decided under the now repealed RSC, under the CPR costs and appeal regimes or in connection with costs awards made before the Act came into force will usually have no relevance for an arbitrator considering a costs question or for a court when considering whether leave to appeal should be granted from a costs award or when considering such an appeal.

35. Rule 13 of CIMAR does not materially alter or gloss an arbitrator's statutory costs powers provided by section 61 of the Act. However, it provides in clear and practical language a detailed and helpful framework governing the award-making process by which an arbitrator's costs powers are to be exercised. Although the wording and effect of rule 44.3 of the CPR is similar to that of Rule 13 of CIMAR, a detailed comparison of the two rules is not helpful when considering the meaning and effect of Rule 13 since the relevant cost powers of an arbitrator conducting an arbitration under CIMAR are to be found exclusively in Rule 13 of those rules.

6.2. The Nature of a Costs Appeal

36. When considering any complaint about a costs award, the court is embarking on an appeal, it is not undertaking a general review of the exercise by the arbitrator of the use of his discretion as to the award of costs nor of the process by which that award was made. For the complaint to arise in the form of an appeal, it must be one that can be expressed in the form of a clear question of law. Often, however, the complaint will be to the effect that the procedure used by the arbitrator was defective or that the decision he arrived at was wrong because of an error in his appreciation or understanding of the material used as the basis of the award. Such a complaint cannot be addressed at all unless it amounts to one of serious irregularity since it does not give rise to a question of law but, at best, gives rise to an attempt to review the costs award.

37. However, where an arbitral tribunal is given jurisdiction to exercise a discretion, the decision making process must be made in accordance with the powers given to the tribunal. The arbitrator must not take into account matters which the law or the powers given him by the parties or the general law preclude him from acting on and, conversely, he must not fail to take account of and give effect to matters that the law requires him to take account of. Moreover, since the tribunal must observe and give effect to the law, the overall discretionary exercise must not be perverse nor one that a reasonable arbitration tribunal properly directing itself could not have reached. These criteria are similar to the so-called ***Wednesbury*** principles applicable to the potential review of the exercise of discretion by an administrative body or tribunal and the so-called ***Birkett v James*** principles applicable to the potential review by an appellate court of the exercise of judicial discretion at a lower judicial level. The question of whether these principles were followed or breached by an arbitrator has always been regarded as one of law, since it raises a question of jurisdiction or one as to the correct exercise in accordance with law of an arbitral tribunal's powers.

[7] Section 1(c) of the Act.

6.3. Question of Law or Question of Fact

38. Any complaint about a costs award that may be made the subject of an appeal must raise a question of law, or the legal part of a mixed question of law and fact. No appeal may be brought on a question of fact. It is never easy to define what is meant by a question of law in the context of an arbitration appeal. Some guidance may be obtained from a consideration of what has been held to be a question of law in related fields where appeals or reviews are permitted in connection with questions of law. These include judicial review proceedings and judicial appeals in the tax or planning fields. However, as Steyn L.J. commented in ***Geogas S.A. v Tramno Gas Ltd (The "Baleares"):*** *"what is a question of law in a judicial review case may not necessarily be a question of law in the field of consensual arbitrations."*[8]

39. In the context of a potential costs appeal, a question of law can arise in connection with the construction and true meaning to be given to an applicable rule governing an arbitrator's power to award costs. It can also arise if it is contended that the arbitrator misdirected himself by taking into account factors which he should not have done or by failing to take into account factors he should have done. As Donaldson J. put it in ***Tramountana v Atlantic Shipping:*** *"In reviewing the arbitrator's decision on costs, it is of the greatest importance to remember that the decision is within his discretion and not that of the courts. It is nothing to the point that I might have reached a different decision and that some other judge or arbitrator might have differed from both of us. I would neither wish, nor be entitled, to intervene, unless I was satisfied that the arbitrator had misdirected himself."*[9]

40. However, it will often be difficult to characterise as a question of law a complaint that a particular exercise of discretion or the decision itself was one which no reasonable tribunal could have arrived at. Usually, such a complaint is seeking the impermissible, namely a review of an arbitrator's costs decision, rather than raising a question of law.

41. What is more problematic is whether an appeal can arise when it is contended that there was no basis for, or evidence to support, critical findings of fact. This question was always, prior to the abolition of the case stated procedure, characterised as raising a question of law. Nowadays, it is important to consider carefully the context in which the question arises as to whether or not a finding of fact was based on any evidence. This context can include cases where the relevant finding was of primary fact where it is said that there was no supporting evidence or that the evidence was misunderstood or wrongly believed. Alternatively, the finding may have been an inference that it is said was erroneously drawn from the primary facts or was one involving the application of the facts to a relevant statutory or contractual label such as: "an adventure in the nature of trade" or "frustration".[10] Finally, the finding of fact may have been made as part of the exercise of a discretion as opposed to the determination of an issue arising as part of the substantive dispute. It is also necessary to consider the procedural context in which the question can arise. This can include, in an arbitration context, an appeal under section 69(1) of the Act or an application for leave to appeal under section 69(2) (b) of the Act. In other contexts, the question can arise as part of the judicial consideration of a case that has been stated by magistrates or special commissioners of income tax, as part of an appeal from a judicial discretionary decision or as part of a judicial review hearing.

42. There is no reason why, in an appropriate case, it should not still be possible in an appeal under section 69 of the Act to raise as a question of law the question of whether or not there was any evidence to support a material finding of fact even though an arbitrator is no longer bound by strict rules of evidence.[11] This is because an arbitrator is bound to decide the dispute in accordance with the law chosen by the parties as being applicable. In a domestic dispute, the governing law will usually be the law of England and Wales which does not allow a decision as to a party's rights or obligations to be made where there is no evidence to support that decision.[12] The relaxation of the strict rules of evidence in arbitrations is a procedural provision which would not justify a finding which decides a dispute and which is not based on any supporting evidence at all.

43. Three decisions where brought to my attention where it was questioned whether an appeal can still be brought under section 69(1) of the Act on this ground. These were ***The "Baleares", How Engineering Services Ltd v Lindner Ceilings Floors Partitions Plc and J A Payne Limited v GAJ Construction and another.***[13] These cases show that where the suggested appeal is one attacking a primary finding of fact on the basis of there being no evidence to support it or where an application for leave to appeal is being mounted under section 69(2) (b) of the Act, the decision of the arbitrator will almost invariably be accepted and may not usually be challenged. The parties have entrusted fact-finding functions to the arbitrator and the parties' autonomy must be respected by the court. However, where the finding is one of mixed law and fact[14] or where the suggested error is that the arbitrator's

[8] [1993] 1 Lloyd's Rep 215 at page 231 (CA).

[9] [1978] 2 All ER 870. This case was decided under the pre-1979 Act procedure where costs awards were only susceptible to a misconduct application.

[10] See ***Edwards v Bairstow*** [1956] A.C. 14, (HL) and ***The "Nema"*** [1982] A.C. 724, (HL) at page 738 per Lord Diplock.

[11] Section 34(2) (f) of the Act provides that it shall be for the tribunal to decide all procedural and evidential matters including whether to apply strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material sought to be tendered on any matters of fact or opinion.

[12] For a recent example of this principle being applied (in a successful judicial review of an appeal decision of the Crown Court on appeal from Licensing Justices) see ***R v Warrington Crown Court, ex parte RBNB (a company)*** [2001] 2 All ER 851 at paragraph 39.

[13] ibid.; [1999] CILL 1521, 24 June 1999, Dyson J, TCC, TCC website; Unreported, 16 March 2001; Judge Gilliland QC, Manchester Merchantile List

[14] See ***The "Lucille"*** [1983] 1 Lloyd's Law Reports 387, Bingham J at page 393 affirmed on appeal [1984] 1 Lloyd's Law Reports 245, (CA).

discretionary decision erroneously took into account facts which should not have been taken into account,[15] a question of law can still arise in the context of an arbitration appeal.

44. I conclude that if it can be shown that there was no evidence of any kind to support an arbitrator's finding, including an absence of evidence admissible by virtue of the relaxation of the strict rules of evidence, at least where the finding amounted to the taking into account of factors that should not have been taken into account, or was a mixed finding of fact and law or was part of the exercise of a discretion whose consequent exercise led to an error of principle, an absence of supporting evidence can give rise to a question of law. However, even if the arbitrator's finding was susceptible to an appeal, a court should give full weight to that finding since the arbitrator is the person whom the parties have chosen as the final determiner of fact. Only if that finding is nonetheless both material and clearly lacking any factual basis should a court consider allowing an appeal on the resulting question of law.

6.4. Substantial Error

45. Where a costs award has been the subject of a successful appeal, the court provides an answer to the question of law that has arisen. It does not follow from that that the costs award will invariably be set aside or varied. Even if the appellant has succeeded on the question of law, the court has a discretion as to whether to give effect to that success by disturbing the award. This is because section 69(7) provides that, on an appeal, the court may by order confirm, vary, remit or set aside the award in whole or in part. It follows that if there has been a successful appeal, the court nonetheless has an option to confirm the award. The relevant considerations that a court would take into account when deciding whether to vary in some way the costs award or, alternatively to confirm it notwithstanding the result of the appeal, would include ones of proportionality. In other words, the court would consider the extent by which the reasoning supporting the arbitrator's overall costs award was vitiated by any identified error of law, the extent in financial terms of the costs consequences of any such error and the relative effect that correcting the error of law would have on the costs to be paid or incurred by the appealing party.

7. The Grounds of Appeal

7.1. Introduction

46. I will first summarise the relevant costs provisions that the arbitrator had to take into account when he considered his costs award, being those imposed by the Act and Rule 13 of CIMAR, with the passages on which the appeal is founded highlighted. The arbitrator summarised the material parts of Rule 13 in paragraph 20.00 of his award. In summary, these powers are as follows:

1. The general principle is that costs should be borne by the losing party (Rule 13.1).
2. The arbitrator has the widest discretion in awarding which party should bear **what proportion of the costs[16]** of the arbitration (Rule 13.1).
3. Where an award deals with both a claim and a counter-claim, the arbitrator should deal with the recovery of costs in relation to each of them separately unless he considers them to be so interconnected that they should be dealt with together (Rule 13.3).
4. In allocating costs the arbitrator **shall have regard to any offer of settlement or compromise from either party,**[17] whatever its description or form (Rule 13.9).[18]
5. In allocating costs the arbitrator **shall have regard to all material circumstances[19]** including such of the following **as may be relevant**[19]:
   (a) which of the claims has led to the incurring of substantial costs and whether they were successful;
   (b) whether any claim which has succeeded was **unreasonably exaggerated**;[20]
   (c) **the conduct of the party who succeeded[21]** on any claim and any concession made by the other party;
   (d) **the degree of success of each party** (Rule 13.2).[22]
   6. The arbitrator may determine by award the recoverable costs of the arbitration on such basis as he thinks fit (Section 63 (3)).
7. The arbitrator, in departing from the general principle as to costs, should give reasons for his costs decision which should include an explanation as to the factors taken into account in departing from that general principle, why those factors were considered to be material and relevant and why, in the light of those factors, the order was made in the form it was (Section 52 (4)).[23]

7.2. General Considerations

47. The arbitrator directed that the costs hearing would be conducted on the basis of written submissions. The arbitrator also directed that he would deal with costs in two stages by first deciding in principle who should pay the costs and in what proportions and then deciding all questions arising out of the detailed assessment. This two-stage approach to the assessment of costs was adopted at the request of the parties. The parties exchanged detailed submissions and followed this with a second exchange of reply submissions. It is to be regretted that both

[15] *Everglade Maritime Inc. v Schiffahrtsgesellschaft Detlef on Apen m.b.h., The "Maria",* ibid
[16] Paragraphs 80–81 below.
[17] Paragraphs 61–64 & 68 below.
[18] The remainder of Rule 13.9, concerned with what is to happen if a party recovers less overall than was offered to him in settlement or compromise, was not applicable since FGL recovered more than the sums offered by way of settlement in the various without prejudice offers made by NEL.
[19] Paragraphs 69, 73 & 83 below.
[20] Paragraphs 53–55 below
[21] Paragraphs 72–74 below.
[22] Paragraphs 75–76 below
[23] Paragraph 83 below

parties' submissions failed to deal, in any detail, with the provisions of Rule 13 of CIMAR and concentrated, instead, on the arbitrator's suggested duty to act judicially when considering and making his costs award. Further, the submissions examined in detail many costs decisions that dealt with the way that a court would have dealt with costs in an analogous case under the now defunct RSC. As I have already indicated, none of these submissions were relevant to the arbitrator's task.

48. FGL's submissions, in summary, suggested that the arbitrator should treat the "*event*" for which costs should be awarded as the overall net recovery by FGL and that FGL should recover all its costs of that "*event*". Although the submissions referred to and rejected any approach to the award of costs on an issue by issue basis, no submission was addressed as to any other possible basis for the award of costs, such as by way of proportioning the costs on a percentage basis. The submissions made detailed reference to the settlement offers of both parties in seeking to show that FGL's conduct had been reasonable throughout the arbitration.

49. NEL submitted that the arbitrator should deal with the costs of the claim and the counterclaim separately and that there should be no order as to costs on the counterclaim. NEL supported this submission with copious references to costs cases relating to costs decisions under the RSC and with an argument that the arbitrator should act judicially in awarding costs. In support of its argument that FGL should not recover any of its costs, NEL relied on FGL's alleged minimal recovery and on its conduct which NEL suggested had unreasonably and unnecessarily extended the length of the hearing. The conduct of FGL that NEL referred to included FGL's pursuit of a number of issues that it lost, FGL's conduct during the contract and its unwillingness to settle the counterclaim during the parties' without prejudice exchanges.

50. Both parties' submissions referred to FGL's loss of profit claim. FGL submitted that this had occupied almost no time whatsoever in the arbitration as a whole and was settled promptly once FGL appreciated that it had not been as successful in the arbitration as it had hoped. The cost of pursuing it had been minimal. In reply, NEL submitted that the significance of this claim was in its contributory effect upon the parties being unable to achieve a realistic compromise given that it accounted for almost 50% of the counterclaim. NEL did not explained why or how the exaggerated loss of profit claim contributed to the parties' failure to achieve a compromise of the counterclaim.

51. In his award, the arbitrator first decided to exercise his power to treat the costs of the claim separately from those of the of the counterclaim. In relation to the costs of the counterclaim, it is clear that the arbitrator was particularly influenced by what he regarded as its exaggerated size, particularly in relation to the loss of profit claim, and the consequent effect on any potential settlement.

52. The arbitrator's principal conclusion was that, had the counterclaim been more modest, an earlier settlement could in all probability have been reached and would not have been discouraged. Indeed, in one passage of the award, the arbitrator stated that the size of FGL's claim made it inevitable that a compromise could not be reached. The following extracts of the award show how heavily influenced the arbitrator was by his inference to this effect: *I am persuaded by the evidence presented to me that it was undoubtedly the magnitude of the counterclaim with its complex allegations relating to quality, standards of performance, the contract documentation, the role of the Contract Administrator and JRK which discouraged total settlement. ... I place great weight on the effect of this substantial sum claimed and its deterrent effect on a settlement being reached at a much earlier date. ... FGL had a claim well in excess of £200,000 firmly in its sights. This made it inevitable that a compromise could not be reached and the proceedings terminated. ... The preconceived notion that [FGL] would be awarded an inflated sum for the counterclaim was more significant than the conduct of [FGL] in negotiations.... The scale of the counterclaim did indeed prevent the possibility of sensible negotiations taking place."*[24]

7.3. Ground 1 – The Exaggeration of the Counterclaim which Precluded its Settlement

7.3.1. Introduction

53. The basis of this ground of appeal was that the arbitrator had erred in finding, firstly, that the counterclaim, and particularly the element concerned with FGL's alleged loss of profit, was exaggerated and that, secondly, it was this exaggerated element of the counterclaim which prevented it from being settled either at an early stage or at all. FGL argued, in essence, that these two findings were vital planks of the arbitrator's reasoning to support his unusual costs order and that they lacked any factual basis. Although these two vital findings were clearly linked, I will consider them separately since different considerations apply to each of them.

7.3.2. Exaggeration

54. FGL firstly argued that it was not open to the arbitrator to find that the counterclaim or any of its constituent parts was exaggerated since its percentage recovery was not so minimal as to justify characterising it in this way. Furthermore, the arbitrator's reasoning was circular since he found that the counterclaim was exaggerated because it was so inflated as to deter a settlement and he also found that a settlement was deterred because the counterclaim was exaggerated.

55. I regard the arbitrator's finding that FGL's loss of profit claim was exaggerated to be a finding of fact which cannot be made the subject of an appeal. Although part of the arbitrator's reasoning is circular, he also supported this finding by relying on its size relative to the sum claimed. He concluded that that disparity was sufficient to constitute the claim as one which was exaggerated. The meaning to be ascribed to a simple English word like "exaggerated" when used in the context of an arbitration claim gives rise to a finding of fact. Although

[24] These passages are to be found in paragraphs 27.00, 36.00, 38.00, 45.00, 48.00, 54.00 & 62.00 of the award.

the parties referred the arbitrator to a number of cases involving the question of whether or not a claim was exaggerated, those cases provided no assistance in deciding the question of exaggeration arising in this case. The arbitrator based his exaggeration finding on the totality of the evidence he had considered during the arbitration and on his observations of the parties' behaviour throughout the reference. Even if I had formed an unfavourable view as to this finding, which I do not, I could not entertain an appeal since the finding was clearly supported by evidence and was based on the arbitrator's decision that the facts as found were fairly described by the ordinary word "exaggerated" which is in wide general use.

7.3.3. No Evidence that the Settlement was Precluded

1. No Evidence

56. The second finding of fact is more problematic. The finding that is attacked, albeit that it was repeated with unhelpful frequency in the award in wording bearing different shades of meaning, was essentially that the exaggerated nature of the counterclaim for loss of profit precluded any settlement, whether at an early or a later stage of the arbitration, because FGL held an excessively enhanced belief as to its likely recovery from this claim. The only evidence supporting this finding relied on by the arbitrator was the size of the counterclaim when compared to the sum awarded (for JRK's fees) or agreed (for the loss of profit). This can be seen from other relevant findings that he made: (1) NEL's rejection of FGL's final offer to accept £45,000 plus all its costs clearly showed that there was no possibility of the counterclaim being settled and (2) the sheer magnitude of FGL's counterclaim was what affected any potential settlement.[25]

57. It is also necessary to take account of the only other evidence referred to by the arbitrator in the award that might be said to be relevant to his critical finding. This was contained in the notes taken by the arbitrator at the Preliminary Meeting in February 1999 in which he had recorded that FGL had stated that its counterclaim exceeded NEL's claim by: *"hundreds of thousands of pounds"*. The arbitrator had a clear recollection of this meeting since he referred to it on two occasions in his award.[26] However, neither party had any opportunity of commenting upon the accuracy of that entry and, even if it was accurate, it provided no support for his critical finding since it was not concerned with the reason why the counterclaim did not settle.

58. Despite the number of occasions that the critical finding is repeated in the award,[27] the only support for it is by way of an inference based on the size of the exaggerated claim and on NEL's rejection of FGL's final offer of settlement. This inference is, in fact, an inference which is contradicted by the evidence contained or summarised in the award and by the statements of both parties to which I will now turn.

2. Failure to Take Account of Offers of Settlement

59. FGL contended that the evidence referred to in the award showed that the counterclaim did not settle at any stage simply because NEL was not prepared to make an offer of settlement whose effect would make FGL the net winner of the arbitration since NEL feared that if FGL accepted such an offer, NEL would have to pay the bulk of both parties' counterclaim costs. FGL relied heavily on the settlement offers to support this submission, particularly those occurring once NEL's claim had been settled.

60. The settlement offers were referred to in the award and copies were provided to the court. There were 8 relevant offers, 3 by FGL and 5 by NEL. It is also relevant to consider that an unsuccessful mediation took place in November 1999. The offers were as follows:

1. In June 1999, NEL offered FGL a settlement on terms that FGL paid NEL £17,584.53 and all NEL's costs. This was rejected by FGL with a further offer amounting to an invitation to NEL to put forward a revised offer taking FGL's claims properly into account.
2. In early November 1999, NEL offered FGL a settlement on terms that FGL paid NEL the reduced sum of £10,000 and all NEL's costs. This was rejected by FGL on 12 November 1999.
3. On 12 November 1999, FGL offered to pay NEL £20,000 to settle only NEL's claim with the costs to be determined by the arbitrator. This was not acceptable to NEL.
4. The unsuccessful mediation took place and the proposed hearing was adjourned until late March 2000.
5. In January 2000, NEL offered FGL a settlement on terms that each party should drop its claims and should bear its own costs. FGL rejected this offer.
6. On 1 March 2000, NEL offered FGL a settlement of the claim alone which made a small advance on FGL's November 1999 offer. This offer was accepted by FGL and the claim was settled.
7. On 13 March 2000, FGL offered NEL a settlement of the counterclaim on terms that NEL should pay FGL £45,000 together with all FGL's costs of the arbitration. This was rejected by NEL.
8. On 24 March 2000, NEL offered FGL a settlement in identical terms to its January 2000 offer, namely that each party should drop its claims and should bear its own costs. FGL rejected this offer and the hearing started soon afterwards.

61. It can be seen from this summary that the parties had narrowed the difference on the counterclaim between them to £45,000, being the difference between the last two offers that were made. However, what principally divided the parties was FGL's costs. The inability to agree who should pay those costs was clearly a major factor precluding a settlement.

[25] See paragraphs 22.00, 26.00 & 25.00 of the award
[26] See paragraphs 15.00 & 22.00 of the award
[27] See paragraph 52 above

62. FGL contended that the arbitrator erroneously failed to take the content of these settlement offers into account and, in consequence, failed to comply with Rule 13.9 of CIMAR which required him to have regard to these offers in allocating costs. In the award the arbitrator stated: *"Referring to the 'without prejudice' correspondence, [counsel] maintains that FGL took a reasonable stance. However, I question this assertion and would rather give weight to the sheer magnitude of FGL's counterclaim and its effect upon any potential settlement"*.[28]

In the light of Rule 13.9 of CIMAR, a question of law arises as to whether the arbitrator was in error in leaving these settlement offers out of account when considering why the counterclaim had not been compromised. It is clear that the arbitrator did leave them out of account when reaching his vital conclusion and, given the terms of Rule 13.9, in doing so he fell into error. Had he taken their content into account, he would have appreciated that the parties' failure to settle the counterclaim arose because NEL was not prepared to offer more, by way of a principal sum, that it had recovered on the claim. The details of these offers would also have shown that the inference he sought to make that the exaggerated counterclaim of itself precluded settlement was not one he could properly have made.

3. The Parties Statements

63. It is noteworthy that NEL never suggested in its submissions to the arbitrator that the counterclaim failed to settle because of its size or because of FGL's exaggerated view of the size of its potential recovery. At best, as NEL submitted, the size of the counterclaim was one factor leading to the lack of a settlement. Indeed, NEL accepted, in its answer to FGL's grounds of appeal, the accuracy of FGL's grounds of appeal to the effect that the counterclaim had not settled because NEL was not prepared to offer a larger sum in settlement than it was to recover on the claim because NEL would then risk having to pay all FGL's costs as the "net loser" of the arbitration. The arbitrator himself appears to have accepted that that concern was motivating NEL's conduct in the arbitration. He found that NEL's sole reason for making its section 57 application was in the hope of bringing FGL's recovery down below the sum awarded by agreement on the claim.[29]

No Appropriate Sealed Offer by NEL

64. The arbitrator should also have had in mind that if NEL had indeed been concerned with the exaggerated size of the counterclaim and was potentially inhibited from reaching a compromise because of that exaggeration, it could have given effect to those concerns in the sealed offers that it put forward. The obvious way for NEL to have made an offer to FGL whilst meeting its concern of its being a potential net loser in the arbitration and thus being in danger of having to pay FGL's costs of the counterclaim would have been for NEL to have made a sealed offer to FGL which either reserved the costs to the arbitrator or which made an offer to pay only a defined proportion of FGL's counterclaim costs. Had such an offer been rejected and had the award in favour of FGL been less than the whatever sum had been referred to by NEL in its offer, that success by NEL would have been a significant matter for the arbitrator to take into account in NEL's favour when giving effect to Rule 13.9 of CIMAR and in reaching his decision in the costs award.

5. Loss of Profit Claim

65. It is also noteworthy how little work was undertaken in working up or considering the loss of profit claim. Apart from the insertion into the counterclaim pleading of a bald reference to a claim for £100,000 without any particulars, FGL provided no detail of this counterclaim until it served its accountant's report not long before the aborted November 1989 hearing. NEL did not work on this report and, soon after the proposed November hearing was adjourned, the loss of profit claim was separated from the counterclaim and ordered to be tried at a later stage. The claim only resurfaced briefly as a formal amendment to FGL's pleading when FGL amended its pleadings at the March 2000 hearing to bring them up to date. It would appear from the terms of the offers and counter-offers of each party, if they are had regard to, that the parties regarded this loss of profit claim as a make weight, or at least was one which was not being pursued with any enthusiasm by FGL.

7.3.4. Conclusion as to Whether a Settlement was Precluded by Exaggerated Claims

66. The conclusion to be drawn is that there is no evidence to support the arbitrator's finding that the counterclaim failed to settle because of its exaggerated nature or because of FGL's erroneously exaggerated view as to the counterclaim's likelihood of success. At best, the exaggeration of the counterclaim may have inhibited settlement discussions in the early months after the Preliminary Meeting but it did not thereafter or generally inhibit a settlement. The failure to settle the counterclaim resulted from NEL's decision not to make a settlement offer in any sum that exceed the sum by which the claim was settled so as to avoid the risk of being held liable for all of FGL's costs.

67. Thus, there was no evidence to support the critical finding of the arbitrator that: *"the magnitude of the counterclaim had a deterrent effect on an early settlement"* or any of the similarly expressed and related findings found within the award. It is important to consider the context in which this finding was made.

68. Firstly, it was not a finding of primary fact but was instead an inference drawn by the arbitrator entirely from the fact that the counterclaim was exaggerated. This inference was not one that could reasonably have been made from that factual basis, particularly since it was made without any regard being paid to the contents of the various offers and counter-offers that had been drawn to the arbitrator's attention but which he had stated he would prefer not to give weight to.[30] As a direct consequence, the arbitrator's inference or conclusion was further

[28] Paragraph 25 of the award.
[29] Paragraph 31.00 of the award
[30] Paragraph 25.00 of the award

vitiated by it having been arrived at without regard to relevant and important factors which Rule 13.9 of CIMAR required to be taken into account.

69. Secondly, the finding was made in the context of Rule 13.2 which requires the arbitrator to have regard to all material and relevant circumstances when deciding upon costs. However, the award does not identify the reasons why the inference being made was either material or relevant to the arbitrator's discretionary power enabling him to proportion the costs. In the context of that Rule, the finding was one of mixed law and fact.

70. Thirdly, the finding was not made in the context of a decision reached on the merits of the issues in dispute but in the context of a determination of relevant factors on which to base a discretionary exercise of the power to make a costs award. In undertaking that exercise, the arbitrator had to take into account all relevant matters and was not to take into account irrelevant matters.

71. Taking all these factors into account, the finding is one which is susceptible to an appeal under section 69(1) of the Act. Since it was unsupported by any evidence, it was not one on which the arbitrator should have based the exercise of his costs discretion provided for by Rule 13 of CIMAR. In consequence, that discretion relied on matters that should not have been taken into account and was, in consequence, one which no reasonable arbitrator could have arrived at.

7.4 FGL's Conduct

72. This ground of appeal is based on the finding of the arbitrator that FGL's conduct was the subject of critical comment. The conduct referred to was conduct occurring during the contract and it led to adverse findings against FGL and Mr Berkins in the principal award and to FGL losing some parts of the discrete issues that were determined in the principal award. These adverse findings included such findings as that Mr Berkins erred in not engaging a competent professional to advise on appropriate standards and finishes; in allowing inadequately detailed drawings to be given to NEL; in not involving Mr Little in the administration of the work; in not affording NEL an opportunity to return to site to make good the defects; in the manner in which he procured, organised and supervised the remedial works and in the pre-emptive manner in which he arranged for the destruction of the brasserie floor. The arbitrator appears to have considered that Rule 13 allowed him to take the conduct of FGL during the contract into account in deciding the incidence of costs. He did not make any finding that the conduct about which he was critical had been repeated during the arbitration nor that it had led to a significant increase in the parties' costs.

73. It is clear that the conduct that is referred to in Rule 13.2(c) is the conduct of a party during, and whilst participating in, the arbitration. The Rule refers to "*material circumstances*" and to such conduct of FGL "*as may be relevant*". Thus, the conduct that is referred to is conduct connected with the arbitration and is clearly intended to be of a kind that increases the length of the hearing, unreasonably increases the parties' costs or otherwise adversely affects the time, trouble and expense of those involved. Of course, there may be exceptional conduct occurring during the time when the dispute was unfolding which it would be reasonable to take into account when reaching a decision about the incidence of costs. However, ordinarily, such conduct would not be material or relevant. If it was generally relevant, an arbitrator would not be able to give effect to the general principle that costs should follow the event and should be borne by the losing party but he would instead, in every case, have to consider whether to give effect to the winner's conduct during the course of the dispute.

74. Thus, the arbitrator erred in considering that the conduct of FGL during the contract and the adverse views he formed about that conduct should count against FGL in deciding on the incidence of costs. Had he considered that this conduct should count against FGL, he should have

75. made findings as to why that was so and why the finding was material and relevant to his costs decision. It may be that the arbitrator would have reached a conclusion adverse to FGL on the basis of at least some of the conduct he relied on but he never considered that point since he had already wrongly concluded that it was sufficient merely to make adverse findings about FGL's pre-arbitration conduct in the principal award.

7.5 Factors Wrongly Taken into Account and Wrongly Not Taken into Account

76. FGL submitted that the arbitrator failed to take into account that the costs of the claim had been dealt with very differently by him despite NEL's smaller claim recovery compared to FGL's counterclaim recovery. FGL also submitted that the arbitrator erred in not taking into account that the vast majority of FGL's costs were incurred on the counterclaim which was all that was in issue after 8 March 2000 following the settlement of the claim.

77. These complaints amounted to a complaint that the arbitrator did not take into account the degree of success of each party but they are not, however, borne out by the award. Amongst other findings, the arbitrator concluded that 80% of NEL's preparation time was incurred by reason of the counterclaim, that he would deal with the costs of the claim and counterclaim separately, that NEL had made a very substantial recovery on its claim which was simple in format and presentation and that FGL's success in percentage terms was very much less than NEL's.[31] It follows that I reject the basis of this ground of appeal which obviates the necessity of considering whether their grounds of appeal raise a question of law at all. It is, however, highly doubtful that a question of law is raised by these grounds since any decision to leave these factors out of account as being immaterial or to take them into account as being material would only give rise to a question of fact and discretion which is not susceptible to an appeal on a question of law.

[31] Paragraphs 6..00, 32.00, 65.04 and 48.00 respectively of the award.

7.6 The Arbitrator's Overall Approach in Reaching his Costs Decision

78. FGL's final and overall ground of appeal was concerned with the arbitrator's overall approach to his costs decision. FGL argued that the arbitrator had, in effect, made four errors: (1) that he failed to determine what the "event" was with which he was concerned; (2) that he failed to give effect to the requirement that any adverse conduct by FGL should be material and relevant to the decision to deprive FGL of any part of its costs; (3) that he took into account matters that he should not have taken into account; (4) that he failed to consider whether any need to reduce FGL's costs entitlement should be achieved by a percentage reduction in its costs recovery and (5) that he gave inadequate reasons as to why his adverse findings were material or relevant and as to why the factors relied on had led to the conclusion that FGL should be deprived of all its costs.

79. There is no substance in the first complaint. The "*event*" the arbitrator was considering was the counterclaim in its entirety including the loss of profit claim and its settlement. That is clear from the structure of the award and from the arbitrator's decision to treat the costs of the claim and counterclaim separately. Thus, it is not open to FGL to complain that the arbitrator did not have in mind what event he was concerned with.

80. The second and third complaints, in so far as they have any substance, amount to additional ways of raising the three questions of law that I have already determined in FGL's favour. The arbitrator was not entitled to proceed on the basis that the exaggeration of the counterclaim precluded its settlement and he should have had regard to the offers of settlement. Equally, he was not entitled to proceed on the basis that FGL's conduct during the contract was open to criticism. This was because he had not gone on to make findings as to why these matters were material and relevant to a costs determination adverse to the winner of the "event" in question.

81. The fourth complaint has more substance. The arbitrator acceded to FGL's submission that it would not be appropriate to consider making an issues costs order even though he had found in favour of NEL on a number of the many issues listed by the parties for his determination. The arbitrator reasonably concluded, given the time and difficulty that would be involved, that it would be wrong and disproportionate to attempt to assess costs on an issue by issue basis. However, the arbitrator then gave no consideration to other possible ways of awarding costs. He proceeded on the basis that, since he was not to separate out the costs on an issues basis, he would have to award FGL either all or none of its costs. He adopted this approach because the parties, for forensic reasons, had only dealt with their rival and competing contentions, from FGL, that FGL should be awarded all its costs on both claim and counterclaim and, from NEL, that FGL should be awarded no costs on either claim or counterclaim.

82. In the light of the arbitrator's findings as to FGL's loss on certain issues and his other findings, it would have been open to him to have reduced the costs otherwise recoverable by a defined percentage or to have used his discretion to reduce particular elements of FGL's costs claim during the detailed assessment that has still to come. The arbitrator was given the "widest discretion in awarding which party should bear what proportion of the costs of the arbitration" by Rule 13.1 of CIMAR, a discretion which would have included the award of a percentage of costs otherwise awardable, yet the arbitrator wrongly limited and narrowed his discretionary exercise. In effect, he only considered which party should bear the costs and he did not consider the additional question of whether an order should be made proportioning FGL's costs.[32]

83. This failure would have been even more marked had the arbitrator not also made the further errors of law that I have already dealt with. If a departure from the general principle that the winner of an event should ordinarily recover its costs was appropriate so far as FGL's costs were concerned, it was necessary for the arbitrator first to consider whether it would be appropriate and reasonable to make a costs order proportioning FGL's costs before making one depriving it of all its costs.

84. As to the fifth complaint, the arbitrator did not appear to consider an intermediate award of costs and he gave no reasons as to why it was appropriate, in the light of his findings, to deprive FGL of all its costs of the counterclaim. Furthermore, the arbitrator's detailed reasons did not explain why his findings were relevant and material nor did it link those findings to the costs decision that he made. Indeed, they showed that he had taken into account factors he should not have done and that he had unduly circumscribed his discretion by not considering whether it was appropriate for FGL to recover not all but only a proportion of its costs.

8. Conclusion

8.1 Conclusion as to Arbitration Costs Appeals

85. My overall conclusions are as follows:

1. An arbitrator, in considering and awarding costs, derives his powers and jurisdiction from section 61 of the Act and any procedural rules incorporated into the reference or agreed to by the parties concerned with the award of costs.
2. In considering whether an appeal will lie from an arbitrator's costs award, the court can only consider judicial intervention if the complaint about a costs award raises a question of law or one amounting to serious irregularity. It is no longer appropriate to consider whether or not the arbitrator acted judicially.
3. Neither an arbitrator nor a court considering an application for judicial intervention should ordinarily consider judicial decisions as to costs nor the terms of the Civil Procedure Rules. The relevant matters to consider are the

[32] It is true that in paragraph 30.00 of the award the arbitrator refers to his "absolute discretion". In context, this is a reference to his decision to treat claim and counterclaim separately and to his view that the costs of the counterclaim should be award to FGL on an "all or nothing" basis. This reference, therefore, supports the conclusion that the arbitrator was fettering his discretion by omitting consideration of an intermediate costs award.

terms of the Act, any applicable procedural rules as to costs and any relevant material arising in the reference whose costs are the subject of the arbitrator's costs award.

4. A court should ordinarily only consider a complaint of serious irregularity in relation to a costs award if the subject-matter of the complaint cannot additionally be expressed as a question of law.
5. A question of law arises if the complaint amounts to one that the arbitrator has taken into account factors that should not have been taken into account, has failed to take into account factors that should have been taken into account, has reached a decision based on an error of law or has reached a costs decision which was one which no reasonable tribunal could have reached.
6. A question of law can arise where the costs award has been based on findings or inferences of fact which it is clear from the award and from any documents incorporated into the award were neither supported by any admissible evidence nor were ones that a reasonable arbitrator could have made. This is because the arbitrator has, in such circumstances, taken into account factors, namely the erroneous findings of fact, which he should not have taken into account.
7. In any consideration of an arbitrator's findings of fact grounding an award as to costs, full respect must be given to the arbitrator's findings and to the principle that the arbitrator is given primacy by both the Act and the parties so far as fact-finding is concerned.
8. Reviewable questions of law will not necessarily give rise to a successful appeal. A costs award will only be set aside if it can be shown that, as a result of the errors made by the arbitrator that have been disclosed by the court's answers to the questions of law, it is reasonable and proportionate to interfere with the costs award.
9. Ordinarily, the result of a successful appeal from a costs award will be an order setting aside the award and a direction to the arbitrator to reconsider the costs award in the light of the judgment setting aside the first award.[33]
10. Where leave to appeal from an arbitrator's costs award is required, the potential appeal must, in addition to these requirements, pass the tests imposed by section 69 of the Act as preconditions to leave to appeal being granted by a judge. However, where as in this case, leave to appeal is not required, the court must consider the appeal on its merits in accordance with the principles set out above.

8.2. Conclusion as to the Questions of Law Raised by the Appeal

86. The result of the appeal is that the arbitrator made the following errors:
    1. He erroneously concluded that the magnitude of the counterclaim had a deterrent effect on an early settlement and he wrongly took that factor into account in reaching his discretionary decision as to costs. That factor had a decisive influence in the costs decision he arrived at.
    2. He erroneously failed to have regard to the offers of settlement.
    3. He erroneously took into account FGL's conduct during the contract even though he had not found any grounds that rendered such conduct material or relevant to his costs determination.
    4. He erroneously fettered his wide discretion and failed to consider a proportionate or other intermediate award of costs in favour of FGL.

8.3. Conclusion as to the Appeal

87. It follows that the award that the arbitrator made as to the incidence of costs on the counterclaim cannot stand in its present form since it was fundamentally flawed by these errors of law. The arbitrator both misdirected himself and erred in principle. The costs award was, in consequence, based on reviewable errors and cannot stand in its present form without reconsideration by either the arbitrator or the court. The extent of these errors and the significant potential effect on FGL's costs recovery are such that it is inevitable that the costs award should be set aside and reviewed again from scratch.

9. The Appropriate Order

9.1. The Applicable Law

88. In the light of this finding as to the costs award on the counterclaim, I must now consider what order to make in consequence. It is clear that the errors of law that have arisen vitiate the costs award, particularly since it was grounded in a finding which, in the form it was made, was one that the arbitrator should not have taken into account. My powers as to what I should do in such circumstances are set out in section 69(7) of the Act which reads:

"On an appeal under this section the court may by order –
(a) confirm the award,
(b) vary the award,
(c) remit the award to the tribunal, in whole or in part, for reconsideration in the light of the court's determination,
(d) set aside the award in whole or in part.
The court shall not exercise its power to set aside an award, in whole or in part, unless it is satisfied that it would be inappropriate to remit the matters in question to the tribunal for reconsideration."

89. The only additional guidance provided as to how these powers should be used is contained in the general principle set out in section 1 to the effect that:

"General principles
1. The provisions of this Part are founded on the following principles, and shall be construed accordingly –

[33] See paragraph 91 below.

(a) the object of arbitration is to obtain the fair resolution of disputes by an impartial tribunal without unnecessary delay or expense;

(b) the parties should be free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest;

(c) in matters governed by this Part [ie sections 1–84 of the Act] the court should not intervene except as provided by this Part."

In addition, the Act defines the general duty of the arbitrator in these terms:

"33(1) The tribunal shall –

(a) act fairly and impartially as between the parties, giving each party a reasonable opportunity of putting his case and dealing with that of his opponent, and

(b) adopt procedures suitable to the circumstance of the particular case, avoiding unnecessary delay or expense, so as to provide a fair means for the resolution of the matters falling to be determined.

(2) The tribunal shall comply with that general duty in conducting the arbitral proceedings in its decisions on matters of procedure and evidence and in the exercise of all other powers conferred on it."

90. The decision that I must make is, in summary, whether I should myself consider what proportion of FGL's costs it should be awarded or whether I should remit that question to the arbitrator to decide in accordance with the guidance I have provided in this judgment as to the approach that should be adopted in the light of sections 61 and 63 of the Act and Rule 13 of CIMAR. The award clearly cannot be confirmed in its present form. It would, however, be possible merely to set aside the costs award if I decided that it would be inappropriate to remit it to this arbitrator and also inappropriate for me to vary that award. If I did that, it would be possible for either party to seek a fresh appointment of a different arbitrator to determine the proportions and details of the counterclaim costs award.

91. Thus, I have the jurisdiction and power to vary the costs award. However, given that an exercise of discretion is involved, it would ordinarily be more appropriate to remit that decision to the arbitrator. That course would appear to be more in conformity with the statutory general principle set out in section 1 of the Act and particularly with the principle of party autonomy which it enshrines. In general, a court exercising its statutory supervisory powers over arbitrators and arbitrations ought to seek to give effect to these principles so far as is reasonably possible.

92. It follows that the power to vary ought ordinarily only to be used where the necessary fact finding has already been completed by the arbitrator and the necessary answer is self-evident. Where a further role is to be performed by the arbitrator, particularly if there is insufficient information in the award to enable the court to decide on the appropriate variation to make to the award in the light of its findings on the question of law that have lead to the appeal succeeding, the appropriate remedy would normally be to remit the award for his reconsideration.[34] This approach with regard to a costs award was the one that was followed by Judge LLoyd QC in ***Metro-Cammell Hong Kong Ltd v FKI Engineering plc***, a costs appeal under the 1979 Act brought at a time when the RSC were still in force. Judge LLoyd had allowed the appeal because the arbitrator had disallowed the successful party two-thirds of its costs as a result of taking into account a factor he should not have done and because he had erroneously considered that he had an unfettered or absolute discretion as to costs. Judge LLoyd stated, in varying the costs award rather than remitting it to the arbitrator, and by then awarding the successful claimant in the arbitration and appellant in the appeal all of its costs:

*"The usual practice of an appellate court is to substitute its own discretion where the tribunal below has erred in law, rather than remitting it to the arbitrator. However, I must bear in mind that now "It is generally accepted that those who entrust decisions to arbitrators do so because they wish to rely upon the judgment, skill and fairness of those arbitrators." (The quotation is from the judgment of the Master of the Rolls in **The "Maria"** as the result of decision on the meaning of the Arbitration Act 1979.) So I do not consider that the position of a court hearing an appeal from an arbitrator is necessarily quite the same as the ordinary appellate court.*

[Counsel for the appellant] however submitted that where the outcome of a remission was plain – on the assumption that the arbitrator exercised his discretion in accordance with ordinary principles of law – no purpose would be served by a remission (which would indeed increase further the already substantial costs of this reference by adding to the amount of the arbitrator's fees for dealing with the issues arising after his primary award). In my judgment this submission is correct. Remission is neither necessary nor desirable unless there is to be further consideration by the arbitral tribunal the outcome of which is not certain, ie where there remains matters which if the tribunal properly directs itself in accordance with the answer to the question of law are nevertheless capable of being decided in more than one way ... I am firmly of the view that no useful purpose would be served by remitting the matter to the arbitrator, since he would inevitably arrive at the decision (which any appellate court would also make), namely that the right order for costs in this case is (and would have been) that (the appellant) should have the whole of their costs of the claim and the counterclaim."[35]

93. It is to be noted, however, that the 1996 Act has extended the power of the court with regard to remission. The 1979 Act only allowed the court to remit the award in full whereas the 1996 Act allows the court to remit the

[34] See ***River Plate Products Netherlands B.V. v Etablissement Coargrain*** [1982] 1 Lloyd's Rep. 628 and **Marc Rich & Co AG v Beogradska Plovidba, The "Avala"** [1994] 2 Lloyd's Rep 363.

[35] (1996) 77 BLR 84 at pages 105–106

award in whole or in part.[36] Thus, for the first time, the court may vary part of the award and then remit the award as varied. This is what, in reality, FGL seeks since any variation of the award resulting in a partial award of costs in its favour would have to be followed by a remission of the award as varied so as to enable the arbitrator to undertake a detailed assessment of the proportion of FGL's costs provided for in that varied award. This alteration of the powers of the Court indicates that the court's power to vary has been widened in a significant respect, albeit that that more extensive power should be exercised with circumspection, given the terms of sections 1 and 33 of the Act.

9.2. The Parties' Submissions

94. FGL contended that I should myself determine what if any proportion of its costs it should be awarded. FGL accepts that, ordinarily, I should remit this award if there remains a decision-making process to be undertaken. However, even if this is the case here, this case is none the less an exceptional one to which that principle should not apply. The arbitrator, in erroneously exercising his discretion as to costs, has made serious errors of principle during which he has shown, it was submitted, an adverse view of FGL and Mr Berkins and a predisposition to deprive FGL of all of its costs of the counterclaim. Thus, FGL has a reasonable basis for considering that any subsequent exercise by the arbitrator of his costs discretion might lack objectivity. This view is one that any reasonable observer of this arbitration, if fully informed of the circumstances and contents of the costs award, would also share.

95. FGL also submitted that, since it was accepted by both parties that a remission would result in a complete rehearing of the costs dispute by the arbitrator, a remission would involve further expense and delay whereas I could speedily determine the costs issue on the basis of the materials previously placed before the arbitrator. The previous costs hearing was conducted solely on the basis of the parties' detailed written submissions. Thus, I would not have to make any findings of fact since the factual basis for the exercise of the costs discretion that I would have to make is already set out in the four relevant awards and those written submissions. I would have to perform a similar exercise to that often performed by the Court of Appeal when it sets aside a first instance decision involving the exercise of discretion, particularly one related to costs, and substitutes its own decision.

96. NEL challenged these submissions. It contended that the ordinary approach that I have already summarised should prevail and that since I have not made any adverse or critical findings about the conduct or capability of the arbitrator, the award should be remitted to him so that he retains the discretion that he has been given by the parties to decide what proportion of FGL's costs should be paid by NEL. There is no reason to suppose that he would do anything other than reconsider his exercise of that discretion in the light of the guidance provided by this judgment. In other words, the circumstances are those expressly provided for by section 69(7) (c) of the Act.

9.3. The Section 67(7) Discretion

97. Before dealing with these submissions, I must first consider what factors I should take account of in exercising my discretion as to whether to remit, vary or set aside the award in the light of my decision on the appeal. I must, firstly, seek to uphold the general principles governing arbitration that are enshrined in section 1 of the Act and by which I am bound. The court should, whenever possible, support the arbitral process and the arbitral procedure that the parties have themselves chosen. In doing so, the court should seek to adopt a course for the dispute under appeal which will most likely obtain its fair resolution by an impartial tribunal without any further unnecessary delay or expense. In other words, I must look to the future and seek to adopt a course for the remaining stages of the dispute resolution process which is most likely to achieve these general principles. If that course can be achieved by a remission, that course should be adopted. However, if that course is more likely to be achieved by court intervention, such a course would be preferable. Any decision to intervene under section 69 of the Act should be governed by these general principles.

98. Given the terms of section 1 of the Act, there is no additional need to consider whether and to what extent the process involving the exercise of my discretion should additionally be influenced by section 6 of the Human Rights Act 1998. That section makes it unlawful for a judge exercising independent judicial functions, which would include the exercise of this discretion, to act in a way that is incompatible with the European Convention on Human Rights. The relevant provisions of the Convention are contained within Article 6. They provide that parties are entitled, in the determination of their civil rights, to a fair hearing within a reasonable time by an independent and impartial tribunal established by law. In agreeing to arbitrate their disputes, the parties may be taken to have waived most of their Article 6 Convention rights. However, the court in acting in a supervisory role, must still, so far as is possible, itself act in a way that is compatible with the Convention. In this case, that would involve my seeking to ensure that the outstanding costs determination is resolved by a fair hearing and by an impartial tribunal within a reasonable time. These are the same considerations as arise from the application of section 1 of the Act. Clearly, in deciding what these terms mean in the context of this arbitration application, I should have regard to the meaning attributed to them in a Convention rights context.

99. The Court of Appeal has, ***In re Medicaments and Related Classes of Goods***[37] recently reconsidered the requirement that a tribunal should be impartial in the light of the Human Rights Act 1998 and, having done so, it ordered the

[36] Section 1(2)(a) of the Arbitration Act 1979 provided that, on the determination of an appeal, the High Court might: *"confirm, vary or set aside the award or remit the award for the reconsideration of the arbitrator together with the court's opinion on the question of law which was the subject of the appeal."*

[37] .[2001] 1 WLR 700, (CA). The court of first instance, the Restrictive Practices Court, sat as a tribunal of three being a High Court judge and two lay members. The complaint related to the conduct of one of the lay members and the effect of the Court of Appeal's judgment was that that

Restrictive Practices Court to recuse itself. The governing principles, set out by Lord Phillips of Worth Maltravers MR delivering the judgment of the court, is as follows:

"We would summarise the principles to be derived from this line of cases as follows. (1) If a judge is shown to have been influenced by actual bias, his decision must be set aside. (2) Where actual bias has not been established the personal impartiality of the judge is to be presumed. (3) The court then has to decide whether, on an objective appraisal, the material facts give rise to a legitimate fear that the judge might not have been impartial. If they do the decision of the judge must be set aside. (4) The material facts are not limited to those which were apparent to the applicant. They are those which are ascertained upon investigation by the court. (5) An important consideration in making an objective appraisal of the facts is the desirability that the public should remain confident in the administration of justice.

*This approach comes close to that in **R v Gough** [1993] AC 646 (HL). The difference is that, when the Strasbourg court considers whether the material circumstances give rise to a reasonable apprehension of bias, it makes it plain that it is applying an objective test to the circumstances, not passing judgment on the likelihood **that** the particular tribunal under review was in fact biased.*

... The court must first ascertain all the circumstances which have a bearing on the suggestion that the judge was biased. It must then ask whether those circumstances would lead a fair-minded and informed observer to conclude that there was a real possibility, or a real danger, the two being the same, that the tribunal was biased."[38]

100. FGL did refer to what was submitted to be a comparable exercise of discretion in an arbitration application context: ***Hagop Ardahalian v Unifert International S.A.***[39] That was a case of misconduct decided under the Arbitration Act 1950. The case involved an application to set aside an award because the arbitrator had expressed a view in his award as to what his decision would have been, had he decided it, on an issue still to be determined in a subsequent award. This comment was found to amount to a decision on a matter that he had not been asked to decide and it amounted to technical misconduct and the award was set aside. The applicant then sought an order removing the arbitrator rather than one remitting the award to the same arbitrator on the grounds that it had lost all confidence in the arbitrator. The Court of Appeal, on the facts, held that remission was still appropriate but it did so having applied this test that was adumbrated by Ackner L.J. in his judgment: *"Do there exist grounds from which a reasonable person would think that there was a real likelihood that [the arbitrator] could not, or would not, fairly determine the safe port issue on the basis of the evidence and arguments to be adduced before him? It seems to me that that is a satisfactory way of expressing the objective test which, to my mind, is the appropriate approach."*[40]

The court declined to remove the arbitrator because it concluded that all the arbitrator was doing was to provide a preliminary indication of what his view might be, subject, of course, to further argument, in order to assist the parties as to whether they really wanted a full-dress hearing involving additional expense at a later stage. Unfortunately, in error, the language adopted in the award went too far. However, that mistake was insufficient to lead a fair-minded bystander to conclude that the arbitrator, a well-known and highly experienced arbitrator in his field, could not deal with the remitted dispute with a fair and open mind.

101. I regard the tests annunciated in these cases to be comparable and that both are applicable to this case. In exercising my discretion, therefore, I must consider, on the basis of the material before me and, in particular, the language and conclusions set out in the arbitrator's reasons supporting award no. 5, whether an objective bystander might reasonably conclude that there would be a real possibility that FGL will not obtain a fair and impartial rehearing of its costs application. In considering that question, I stress, as did the Court of Appeal in the ***In re Medicaments and Related Classes of Goods*** case, that I am not concerned to pass judgment on the likelihood that this particular arbitrator would in fact be biased. The test is what the reasonable observer might conclude as being a real possibility.

9.4. Remission, Variation or Setting Aside

102. The costs award of the arbitrator was vitiated by a number of serious errors of law. The crucial and erroneous finding that the exaggerated size of the counterclaim was such as to make its settlement impossible or extremely unlikely, was repeated on eleven occasions in the award. The relevance and materiality of some of the crucial findings to the decision that FGL should recover none of its costs was not identified and the reasoning supporting the decision to deprive FGL of all, as opposed to some, of its costs was based on more than one error of law. These were not merely technical or formal errors. They were made in relation to what had become by far the single most significant issue, as to costs, on which most of the very considerable financial consequences of the arbitration turned. Any tribunal asked to reconsider afresh its exercise of discretion in such circumstances would have difficulty in retaining the confidence of both parties, the more so given the nature and extent of the errors that have led to the need for a fresh consideration. That is why, ordinarily, an appeal court itself re-exercises a procedural or costs discretionary exercise if it has set aside the first instance decision as having been exercised on the wrong grounds. I am satisfied that FGL has shown that a remission might well result in the resulting costs rehearing failing to meet an objective test of impartiality and fairness.

member should have recused herself. This case was not cited in argument but it confirms and states in authoritative terms the governing principle that FGL contended as being applicable.

[38] Paragraphs 83–86 of the judgment of the court.

[39] [1984] 2 Lloyd's Rep. 84, (CA).

[40] At page 89 (left hand column).

103. A particular reason for this conclusion is that the rehearing, whether by the court or the arbitrator, would have to restart from scratch. I could give detailed directions as to how that hearing should be conducted and as to the extent to which fresh material and arguments could be relied on by both parties. Indeed, both parties agree that a rehearing is needed. If, objectively, there are grounds for concern that, at the first hearing, the arbitrator showed a potential predisposition to find against FGL, such grounds would be reinforced at any such rehearing, even if it was conducted without any error of law.

104. In these circumstances, none of the relevant factors that I must take into account would suggest that a remission is appropriate since it would have the potential for both unfairness and a lack of impartiality. A remission would also incur the additional costs and delay of a rehearing before the arbitrator, which would have to be concluded within three months, with the potential for yet further costs and delay in a possible subsequent court challenge of the new award. On the other hand, I can take the necessary decision within a few weeks, confining myself to the material now on the record and to a short hearing. This would not involve me in any fact-finding exercise and would involve a discretionary weighing up of all the relevant and material factors and then forming a view as to the reasonable proportion of FGL's costs (if any) that it should recover.

105. The exercise of varying the award will be one which will involve a consideration of what proportion of FGL's costs incurred on the counterclaim should be recoverable. No possible answer to that question would be ruled out in advance so that the final decision could be anywhere in the range from 100% to nothing. If that latter course was decided upon, the variation to the award would be to the effect that: *"The court having reconsidered what costs should be recovered, it is confirmed that the each party should bear its own costs of the counterclaim."*

Thus, the exercise by the court of a discretion would conform to section 70(2) of the Act which provides that, where the award is varied, the variation has effect as part of the award.

106. Having reached this conclusion, I must finally consider whether I should vary the award or set it aside and leave the costs decision to be taken by a freshly appointed arbitrator. That course would maintain the primacy of the parties' decision to have their disputes resolved by arbitration but would involve even greater expenditure and delay than a remission. Thus, although the statutory precondition for setting aside, namely that it would be inappropriate to remit that question for reconsideration, has been met, variation remains a more satisfactory option to setting aside.

107. The further question is whether it would be appropriate for the arbitrator to retain jurisdiction to assess the detailed costs of the claim and the counterclaim under section 63 of the Act and Rule 13.10 of CIMAR once the award, as varied by me, has been finalised. Both parties suggested that it would remain appropriate for the arbitrator to conduct this final stage of the dispute even if I had previously conducted a variation hearing of the costs award. I agree with this jointly held view.

10. The Proportion of FGL's Costs of the Counterclaim

10.1. Overriding Considerations

108. In considering what proportion of its costs FGL should be entitled to recover, a number of salient facts relating to the overall nature and conduct of the arbitration must be kept in mind. Essentially, the arbitration arose out of disputes as to the quality of the kitchen and brasserie floors constructed by NEL for FGL. These disputes were wide ranging in that they covered: (1) factual disputes as to who undertook the design of the floors; (2) what NEL's contract obligations were, particularly as to the materials to be supplied and the falls to which the floors were to be laid; (3) who was the supervising officer and what approval that person had given to the quality and finish of the floors; (4) whether the works, particularly the floors, had achieved practical completion and, if so, when; (5) what defects and design deficiencies the floors had; (6) what remedial work was reasonably necessary, whether NEL had been given a reasonable opportunity to undertake that work and whether it had been prepared to do so; (7) what the reasonable measure of damages was for NEL's proved breaches of contract and what damages should be awarded; (8) what liquidated damages FGL could recover for the remedial work and for alleged loss of profit flowing from the defective work and (9) the reasonableness of the professional fees charged by JRK in its investigations and in the supervision of the remedial work that was undertaken by other contractors.

109. The nature of these disputes and their close inter-relatedness led the parties, against the wishes of the arbitrator, to agree to apply jointly for an adjournment of the hearing and to press for a refixed hearing devoted to all issues. This request was made because both parties accepted that the issues had to be heard and determined together. However, soon afterwards, the parties and the arbitrator all agreed to hive off the loss of profit claim since that raised discrete issues which might never arise and which could and should be dealt with separately. Following that decision, neither party incurred any further costs on that issue, indeed save for minimal expenditure by NEL, only FGL had incurred any costs at all on that issue.

110. The parties made several unsuccessful attempts to settle all counterclaim issues including, at a late stage, a mediation exercise. Sealed offers were made, on NEL's side with the intention throughout that it would not offer more than it either thought it would recover or that it had recovered, on the claim. NEL never gave thought to making an offer on the counterclaim exclusive of costs or which left the award of costs to the arbitrator.

111. The decision to identify issues was made by the parties at a late stage and the list of issues was presented to the arbitrator as an agenda for the hearing. This was a convenient way of focusing the evidence, submissions and the award but, overall, NEL's claim dealt with at the hearing was a monetary claim for damages based on repair

costs and for JRK's fees. The loss of profit claim remained effectively stayed pending an award on these other claims.

112. The arbitrator found for FGL on certain crucial issues, particularly on the need to relay the floors and on its entitlement to recover damages based on the cost of employing other contractors to do the work. Hence, NEL lost on the issue that it should have been able to repair the floors and that FGL's damages should be limited to the notional cost of NEL undertaking those repairs. NEL won on issues relating to the use of concrete drainage channels, whether or not the floor should have been laid to floors and as to the dates of practical completion. On the issues of design and supervision, the result was effectively a draw with FGL winning on the question as to whether the work had been approved by FGL's supervisor (it had not) and NEL winning on the issue of who was the supervisor.

113. The arbitrator made adverse comments about the conduct of FGL's principal witness, Mr Berkins, during the course of the work. Moreover, the nature of his evidence, much of which the arbitrator did not accept, required additional witnesses and hearing time which would have been saved had his recollection of events been more accurate.

114. There was only one discrete issue which did not clearly interlink with the mass of floor issues. That related to the reasonable fees that JRK could charge. The arbitrator reduced this head of claim substantially but the overall hearing time devoted to it was not great.

115. The arbitrator decided to separated the costs of the claim from the counterclaim. Given the separate nature of the claim from the counterclaim and the relatively small amount of costs that must have been expended by each party in preparing for and ultimately settling the claim, this was clearly a reasonable decision for the arbitrator to have taken.

10.2. NEL's Objections

116. NEL put forward four grounds for seeking an order relieving it of any costs liability and in support of the arbitrator's costs award.

1. NEL's Relative Success

117. NEL contended that it had won on five of the seven issues determined by the arbitrator. This contention overlooked the fact that the list of issues had been prepared at a late stage of the arbitration and had been prepared by both parties as a means of focusing the minds of the parties and the arbitrator at the hearing. The issues were, in truth, topics to be covered by the evidence and they set out certain key areas where factual findings would be required of the arbitrator. These issues did not refer to the voluminous schedule of defects which the arbitrator also had to make findings about. The issues were not, therefore, discrete nor were they readily identifiable component parts of the counterclaim disputes. NEL's further difficulty was that it was impossible for it to give any clear or meaningful indication, even in outline, of how much of the hearing time or of the pre-hearing costs had been devoted to the issues which it claimed to have won. Finally, its so-called victories were not clearcut, even on the issues it claimed to have won. It follows that a small but not readily identifiable proportion of FGL's costs were incurred in dealing with disputed issues and facts on which it lost and that a small reduction in FGL's recoverable costs would be appropriate on this ground.

2. Exaggerated Claims

118. NEL relied on the finding of the arbitrator in his costs award to contend that FGL had greatly exaggerated the claims it was making. In essence, the claims referred to were the loss of profit claim and the claim for JRK's fees. The other claims were not exaggerated although they were marginally reduced in the award. This relative lack of reduction on the defects claims arose because of the arbitrator's finding that the costs of repair could reasonably be related to the costs incurred in employing other contractors. This finding was not appealed by NEL.

119. Clearly, an exaggerated claim can reasonably lead to a reduction or total elimination of a successful party's costs. However, ordinarily, any exaggeration must be shown to have led to an unreasonable increase in costs or to have acted as an unreasonable stumbling block to settlement. In this case, the parties attempted mediation, made several settlement offers to each other and hived off for separate determination the largest claim at an early stage. Overall, the real battle on the counterclaim related to FGL's claims for defective work. Thus, a relatively small reduction in FGL's recoverable costs is appropriate as a result of its exaggeration to take account of the marginal increase in both parties costs occasioned by the exaggeration that occurred and to mark the possible hinderance to settlement discussions that that exaggeration might have created.

120. It follows that some relatively small reduction of FGL's costs should reasonably flow from the exaggerated elements of its claims but that that reduction should be narrowly confined.

3. Mr Berkins' Conduct

121. I have already summarised this complaint. Mr Berkins' conduct during the work was unreasonable and no doubt exacerbated the tense relationship that developed between the parties and his evidence also increased the length of the hearing and the preparation costs. However, the respects in which he was criticised cannot be said to require more than a modest reduction in FGL's costs recovery. Much of the criticism contained in the award was a direct corollary of the adverse findings of fact that were made by the arbitrator which, in turn, were a necessary concomitant of a disputed arbitration which had within it a complex factual background that had to be unravelled.

4. Cost of the Special Damages Claim

122. Costs were incurred by FGL in preparing its accountant's report which was served at a relatively late stage and was then never used. FGL should reasonably bear its own costs of arranging for the preparation of this report.

10.3. Conclusion

123. On analysis, NEL was principally seeking to reinstate the arbitrator's reasoning which had been so heavily based on the arbitrator's erroneous finding that FGL's conduct and its exaggerated claim had led to a situation in which it was impossible for the arbitration to be settled. If those aspects of FGL's conduct that it is reasonable to refer to and take into account are given effect to, I conclude that FGL should recover about two thirds of its costs and should bear all its accountancy expert's costs. In order to provide a reasonable and workable figure, I have rounded the recoverable percentage of FGL's costs down to 65%.

11. Certificate and Leave to Appeal

124. NEL seeks leave to appeal the principal questions of law that I have determined. This application is made under section 69 (8) of the Act which provides that: *"... no ... appeal [to the Court of Appeal] lies without the leave of the court which shall not be given unless the court considers that the question is one of general importance or is one which for some other special reason should be considered by the Court of Appeal."*

125. It is clear from the decision of the Court of Appeal in ***Henry Boot Construction (U.K.) Ltd v Malmaison Hotel (Manchester) Ltd.***[41] that this section involves a two-fold decision by me and that neither decision is subject to further review by the Court of Appeal if I decide either against NEL. I must decide whether permission to appeal should be granted (the "permission test") and I must also decide whether the disputed question or questions of law are ones of general importance or are ones which for some other special reason should be considered by the Court of Appeal (the "Act test"). Section 69 (8) of the Act changes the position from that pertaining to arbitration appeals under the 1979 Act. Under the previous practice, it was for the judge at first instance to certify that a question of public importance was raised and the refusal of such a certificate was conclusive and not renewable in the Court of Appeal. However, the subsequent grant of leave to appeal, if a certificate was given, was for either the judge at first instance or for the Court of Appeal if leave was initially refused by the judge.

126. I regard the two tests as being closely inter-linked and to be decided together albeit that they are separate hurdles for NEL to overcome. Furthermore, I regard the permission test as to whether there should be permission to appeal as being similar to the test imposed on potential litigants seeking permission to appeal a final judgment to the Court of Appeal under the CPR. That test requires the judge, or the Court of Appeal, to be satisfied that the appeal has a real prospect of success or that there is some other compelling reason why the appeal should be heard.[42]

127. Since FGL's first appeal to the TCC was brought without the need for leave to have first been obtained, the relevant questions of law were never clearly spelt out. The questions of law must be ones: "arising out of an award made in the proceedings". The wording of the questions of law that arise were the subject of some debate and this wording was never finally settled. I believe that the questions that have arisen during the course of this appeal are, in summary:
    1. What is the correct test for an arbitrator to apply when considering an award as to costs?
    2. What is the correct test for the court to apply in considering whether a question of law arises out of a costs award?
    3. Are findings or inferences of fact that were relied on by the arbitrator as the basis of his costs award which were not supported by any evidence capable of giving rise to a question of law? Did the arbitrator, in relation to the disputed findings of fact, take into account matters he should not have done, fail to take into account matters he should have done or otherwise reach a decision that no reasonable arbitrator could have arrived at?
    4. Is the award of the arbitrator one which took into account matters it should not have done or failed to take into account matters it should have done?
    5. In the light of the answers to the questions of law, should the costs award be set aside?
    6. If the costs award is set aside, should the award be remitted or varied? In deciding that question, how should the discretion provided by section 67 (7) of the Act be exercised?

128. It can be seen from my judgment that the first three questions of law give rise to general questions of law which arise for determination under the Arbitration Act 1996 for the first time and which have a considerable bearing on arbitration costs hearings and on costs awards appeals, particularly for the many construction arbitrations conducted under the CIMAR Rules. Any judgment of the Court of Appeal will be reported and will be available for general consideration and guidance. Such guidance will be welcomed by the construction arbitration community.

129. Furthermore, the sixth question raises a significant question of principle as to the significance to be given by the court to potential unfairness to one party if there is to be a remission when it exercises the wide powers given to it by section 67 (7) of the Act following a successful appeal.

[41] [2000] 3 WLR 1824, C.A.

[42] CPR 52.6

130. There is no reported authority concerned with these questions. However, they are of some importance, particularly where the parties do not require leave to appeal, which is a situation which occurs with some frequency in construction arbitrations.

131. I am therefore satisfied that the general questions of law are ones which satisfy the Act test that there should be a special reason for giving leave to appeal pursuant to section 69 (8) of the Act. If these questions are to be made the subject of an appeal, it will be necessary for the Court of Appeal to have before it the facts and circumstances of this case and, in consequence, the remaining questions need to be considered as well and should, in consequence, also be permitted to be made the subject of a second appeal to the Court of Appeal.

132. Since this is my view when considering the Act test provided for by section 69 (8), it would be nonsensical, as I see it, if I then concluded that the permission test was not satisfied. In other words, I cannot, reasonably, decline to certify that there are other compelling reasons for a second appeal.

133. I should record that NEL, in seeking the appropriate certificate, did not include the sixth question within its application but, since I am certifying the other questions, it is right that I should include this question too and leave it to the parties, if a second appeal is brought, to decide whether to pursue that question as well.

134. Since I have concluded that this case and the questions of law that I have been concerned with merit a certificate on broad public interest grounds, there is no need for me to express any view as to the prospects of success that any such appeal might have and I do not do so.

135. I conclude that leave to appeal under section 69 (8) of the Act should be given to NEL for all the questions of law that have arisen on the hearing of this appeal.

12. Assessment of Costs of the Section 69 Arbitration Applications

136. I have carried out a summary assessment of costs using a schedule prepared by the parties which sets out the costs claimed by FGL and the responses of NEL to each item in the schedule that was disputed. My assessments were set out in that schedule which was provided separately to the parties.

13. Overall Conclusion

137. The appeal will be allowed. The arbitrator's costs award will be varied pursuant to section 69 (7 (b) of the Arbitration Act 1996 so that NEL is to pay FGL 65% of its costs of the counterclaim. Such costs are not to include the costs of and associated with the expert accountant's report. Failing agreement, such costs are to be taxed by the arbitrator. NEL shall have the leave of the court to appeal to the Court of Appeal pursuant to section 69 (8) of the Arbitration Act 1996 the questions of law set out in paragraph 126 above.

Richard Fernyhough QC and Simon Hargreaves (instructed by Eversheds, Manchester) for FGL.
Nicholas Dennys QC and Andrew Burr (instructed by Nelsons, Nottingham) for NEL.