DOSSIERS
ICC Institute of World Business Law

Third-party Funding in International Arbitration

INTERNATIONAL CHAMBER OF COMMERCE

Edited by
Bernardo M. Cremades,
Antonias Dimolitsa

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Foreword

Yves Derains

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That there is no such thing as a free lunch remains a debatable statement. But that there is no such thing as a free arbitration is not. The issue is not whether or not arbitration is more expensive that litigation, in particular in the light of the success of the Report on Techniques for Controlling Time and Costs in ICC Arbitration.* The respective costs of litigation and arbitration depend mainly on the characteristics of the legal system of each country, on the complexity of each case as well as the possibilities of recourses existing in each jurisdiction. The issue is that, as a form of private justice, arbitration is meant to be exclusively financed by the parties. This does not apply to litigation. As access to justice is a constitutional right throughout the world, ways and means have been devised in order that this right might be exercised in national courts. They are not always very efficient but at least the concern is universally shared. On the contrary, an impecunious party to an arbitration agreement may be *de facto* deprived of the right of access to justice when it is unable to sustain the costs of the arbitration procedure. In the *Pirelli* case, for example, the Paris Court of Appeals in November 2011 set aside an ICC award because of the arbitral tribunal's refusal to deal with counterclaims due to the respondent's failure to pay the special deposit applicable to them, on the grounds that this was at odds with the right of access to justice and the principle of equality among the parties. The French Cour de Cassation annulled this decision in March 2013,† but only because the Court of Appeals had not checked whether the counterclaims were really intertwined with the claimants' claims, admitting that – if such had been the case – the right of access to justice and the principle of equality would actually have been breached. Thus, the tension between the need to finance arbitral proceedings and access to justice is not an abstract issue.

Third-party funding of arbitration offers a solution to this irritating problem. It is a scheme where a party unconnected to a claim finances all or part of one of the parties' arbitration costs, in most cases the claimant. The funder is remunerated by an agreed percentage of the proceeds of the award, a success fee, a combination of the two or through more sophisticated devices. In the case of an unfavourable award, the funder's investment is lost. Such arrangements, said to originate from Australia where they appeared in the 1990s, are made with specialized finance corporations that have their biggest markets in the UK and the US. However, since 2010, they are operating worldwide, both in common law and civil law countries.

Situations where a claimant is not personally financing its claim are not unheard of. It happens when an insurer has already compensated a party for its damages (or a substantial part thereof) on the condition that the party files an arbitration claim against the author of the damage. Likewise, a claimant is not financing its case when its counsel is working on a contingency fee basis. However, beyond the fact that the claimant is not personally financing its claim, such situations have very little in common with third-party funding. The insurer is financing a claim in order to recover the money it has paid out. The attorney working on a contingency fee basis is primarily financing his or her representation activities, before receiving a success fee. Third-party funding is an investment per se in arbitration by a corporation specialized in this business. It should come as no surprise that, as any new novelty, third-party funding has been and remains controversial. In common law countries, medieval concepts such as maintenance and champerty were even referred to, although, in modern times, their only function is to protect uneducated persons ignorant of the availability

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* ICC publication no. 861E.

† Cass. Civ. 1er, March 28, 2013, nº 392 (11-27.770).

of legal aid, which, as mentioned above, does not exist in arbitration! In civil law countries, the old principle *nul ne plaide par procureur*, which requires anyone acting as a plaintiff or defendant in a lawsuit to make his identity known individually in the legal proceedings, was opposed to third-party funding, although it hardly seems applicable in the circumstances, as the funder is not acting in the arbitration. It does not buy the claim, it finances it. The suggestion that third-party funding might encourage frivolous claims was also made, without considering that no serious corporation would finance a claim without being convinced through due diligence that it has a good chance of success.

All this merits little concern given that there is no doubt that third-party funding allows easier access to arbitration for impecunious claimants with meritorious claims, and, as such, represents progress. Yet, one must not ignore the difficulties generated by the involvement of a funder in arbitration, due to the specificity of arbitration proceedings. Third-party funding raises ethical issues relating to the level of independence of counsel in the control of the proceedings and in particular in the choice of the arbitrator. Can an arbitrator act in a case where the claimant is financed by the same third-party funder who is also financing a different claimant in another case in which a partner of the law firm of the arbitrator is acting as that claimant's counsel? As long as the intervention of the third-part funder is not disclosed, the matter may raise serious concerns.

This is only one of the many sensitive issues that were discussed by advocates, arbitrators, experts, scholars and, above all, representatives from some major third-party funding corporations at the 32nd Annual Meeting of the ICC Institute of World Business Law on November 26, 2012. The programme, prepared with efficiency, diplomacy and great intelligence by Antonias Dimolitsa, Vice-Chair of the Institute, and Bernardo Cremades, one of the very active members of its Council, is at the origin of this Xth Dossier of the Institute. There is no doubt that it will be a masterpiece in the collection.

Yves Derains

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Introduction

Antonias Dimolitsa*

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The rise of third-party funding in international arbitration is a reality, and has been the subject of many conferences, articles and roundtables over the past four years. Recently, entire books have even been published on this subject. A significant number of parties in international arbitrations, whether or not in financial distress, are today financed by professional funders, and the demand for such funding apparently outstrips the supply. These parties – mostly claimants but also respondents – originate not only from Australia, Canada, the United States and the United Kingdom but also from civil law countries. A lot of issues, however, with tangible hazards regarding both the functioning of this new funding industry and its impact on the arbitral process remain open and are even growing. On the one hand, reluctance and criticism still exist, even in fora like the US Chamber of Commerce; on the other hand, case law is evolving towards acceptance of third-party funding and is beginning to resolve some salient issues in this field. The ICC Institute of World Business Law, with its think-tank role, could obviously not ignore this overwhelming development in business law and international arbitration.

We organized the 32nd Annual Meeting of the Institute with a view, first of all, to achieving a better understanding of the reasons for the expansion of this funding industry by distantiating it from its origins, comparing it to other funding mechanisms and, in particular, examining its special features as an investment process. All these issues were covered during the morning sessions, where the focus was on the funding industry and its specificities and the underlying aim was to reconsider any legitimate doubts that we might have in this respect. Second, during the afternoon sessions, the aim was to explore the status of third-party funders and the possible complications that their presence may bring about in the arbitration process from the point of view of both counsel and the arbitral tribunal. Third-party funder's involvement in the post-arbitral phase was also discussed. In addition, special attention was given to investor-state arbitration, and several much discussed precedents were considered. The focus was the impact of third-party funding on arbitration, and the underlying concern was the preservation of the integrity of the arbitration process.

The present volume of the Dossiers includes the contributions of most of the speakers at the Annual Meeting. On the subject of the third-party funding industry *per se*, **Georges Affaki** explains its characteristics as a financing business, including its rules, risks and limits, and discusses some rules of governance, posing various questions as a consequence of the *Oxus Gold* case. In a comprehensive overview of third-party funding as a financing industry, **Selvyn Seidel**, initially focuses on the distinct features of third-party funding in relation to international arbitration and urges on developing a record of experience, rules, regulations and guidelines. In a proposed way forward, he also identifies several issues that require early attention. Next, he analyzes the particularities of the investment decision based on the asset class (*i.e.* arbitration claims) and highlights the skills that decision-makers must have, or have available, in order to overcome its "daunting" character. In a new additional paper closely pertaining to the subjects dealt with during the morning sessions, **Selvyn Seidel** and **Sandra Sherman**, also bearing in mind the *Oxus Gold* case, stress the necessity of governance rules for the third-party funding industry in reply to concerns at two levels: first, the need to prevent and/or reduce the risk of illegal conduct by funders; and, second, the need of the funder to assure itself that the claimant has taken proper precautions against illegal activity. They conclude by proposing some rules or guidelines for consideration.

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* Co-Editor, Vice-Chair of the ICC Institute of World Business Law.

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Christopher P. Bogart's aim is to illuminate the advantages that arbitration finance brings to companies and their lawyers by stressing the fact that it allows access to justice, especially in investor-state arbitration, and levels the playing field. He also examines some key issues that preoccupy arbitration practitioners, such as disclosure and the impact of third-party funding on settlement and adverse costs; and he discusses the different forms that third-party funding may take. **Mark Kantor** departs from third-party funding that focuses on claimants and deals with risk-management tools for respondents, specifically two insurance products: "after-the-event" (ATE) insurance for legal costs and "outcome hedging", "caps" or "litigation buyout" insurance (LBI) to create a stop-loss liability (outcomes policies).

Turning to issues that arise as a consequence of the existence of third-party funders in the arbitration process, three contributions deal with such issues in general, while three others deal with them with respect to investment arbitrations.

Charles Kaplan deals with these issues from the counsel's perspective. Counsel may him/herself be a third-party funder, in which case the possibility of the prohibition of contingency fee arrangements in comparative law arises. At the present time, however, the key issues for international arbitration practice concern the relationship counsel/client/professional funder, both during the due diligence process (in view of the conclusion of the funding agreement) and during the arbitration proceedings. The obligation of attorneys to act in the interests of their clients and take instructions only from them certainly applies but may be somewhat nuanced in the presence of a third-party funder. In addition, confidentiality as an obligation towards the client during the due diligence process, as well as professional and ethical obligations towards the arbitral tribunal during the proceedings with regard to disclosure of the presence of a third-party funder may well become problematic.

Disclosure of the existence of a third-party funder is certainly a central and much debated issue. **Laurent Lévy** and **Régis Bonnan** examine the issue from the arbitral tribunal's perspective and show that there is no specific obligation of the funded party to disclose this existence as such; however, other circumstances may sometimes require such disclosure. On the other hand, in the event that the tribunal knows about the existence of a third-party funder, it is improbable that the latter will meet the conditions for being joined to the proceedings as a party. The effect that the third-party funder may have on the admissibility of the claim and the arbitral proceedings triggers a discussion of different legal concepts and procedural mechanisms but does not seem to be of real or specific importance in actual practice. Focusing on disclosure and expressing a somewhat differing opinion, **Maxi Scherer** circumscribes the rationale for a possible obligation to disclose the funding agreement to the assessment of the necessity of ordering security for costs and the avoidance of conflicts of interest. Questions regarding the scope of such an obligation and its modalities do, however, arise, taking into account, *inter alia*, the imprecision of the definition of "third-party funding agreements" and the reluctance of professional funders to disclose the exact terms of funding agreements.

Due to transparency under its different forms, the involvement of third-party funding in investment arbitrations arguably seems most important. Three articles focus on investment arbitration. In their introduction to and overview of the topic, covering issues regarding the implications of third-party funding that are specific to investment arbitration as well as general issues applying to all types of arbitrations, **Carolyn B. Lamm** and **Eckhard R. Hellbeck** also consider potential concerns that a state may have in making use of third-party funding. Contrary, however, to the existing few examples of states making use of third-party funding and notwithstanding such concerns, information exists that the funding industry appears to discern a "clear demand" for respondent funding in investor-state arbitration. **Angelynn Meya** concentrates on the investment arbitration decisions that have assessed the role of a third-party funder from two angles: jurisdictional challenges (questions of standing with regard to the nationality requirement of a BIT or the ICSID Convention and with regard to the real party in interest) and costs and security for costs. Her conclusion is that investment tribunals seem to prefer to ignore the implication of third-party funding. **Antonio Crivellaro** lists and analyzes all publicly known investment arbitrations that involved third-party funding. This paper constitutes an important overview of the subject. He observes that in most cases

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such involvement did not give rise to procedural or substantive obstacles and that international tribunals are generally well disposed towards third-party funding in investment arbitration. In his opinion, disclosure should be mandatory in investment arbitration, in view of the protection of the state and the guarantee of due process. Moreover, he claims that third-party funding should be regulated by a soft-law type of instrument that the parties or tribunals might voluntarily adopt as binding in each individual case.

It appears that there is no clear-cut conclusion to be drawn from the contributions to the ICC Institute of World Business Law's 32nd Annual Meeting. The third-party funding industry continues to be very secretive, and funders are reluctant to disclose, if not their very presence behind an arbitration, then at least the funding agreements they have concluded. Conversely, counsel and arbitrators seem to be in favour of disclosure, yet not as a general, absolute rule. In addition, no consensus exists at all on the need for regulation of third-party funding, and those who are in favour of an international regulation, for example through soft-law instruments such as codes of conduct or guidelines, run up against the issue of enforceability.

In any event, the aim of the Annual Meeting was to consolidate the knowledge in this area in order to better deal with the growing phenomenon of third-party funding in our professional activities, without exaggerating the problems and risks it may generate during this period of unregulated yet overwhelming development. We are left with the impression that the general understanding emerging from this meeting of third-party funding pioneers and experienced arbitration practitioners is that our common interest lies in the direction of a serene coexistence that facilitates the rendering of justice and does not affect the integrity of the arbitration process.

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