THIRD-PARTY FUNDING IN INTERNATIONAL COMMERCIAL ARBITRATION

Master’s thesis in the ‘Master of Laws’ program

Submitted by

Thibault De Boulle

(Student No. 00902551)

Supervisor: Prof. Dr. M. Piers
Commissioner: Prof. Dr. J. Erauw
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“[F]inancing of litigation and arbitration claims by third parties is neither new nor capable of being characterised in the rather black and white manner so often employed by press and academic writing. In reality, the practice is complex and multi-faceted.”

C. Bogart, 2013

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NEDERLANDSE SAMENVATTING VAN DE MASTERPROEF CONFORM ARTIKEL 2.5.3 VAN HET REGLEMENT MASTERPROEF .............................................. 125
This master’s thesis is the final chapter of my law degree at Ghent University. Being drawn to the fascinating world of international commercial arbitration and with a healthy interest in international business, third-party funding (“TPF”) seemed like, and proved to be, a perfectly suitable multidisciplinary subject matter for a master’s thesis.

Writing a thesis on a topic where a substantial part of the available information is dominated by interest groups (i.e. third-party funders) entails some pitfalls. Among other hazards, there is an inherent risk that one could lose its sense of nuance, which could have a detrimental influence on the impartiality of the analysis. Nevertheless, I have tried to stick to the facts and reference the views of both the enthusiastic advocates and the fierce opponents.

Furthermore, this preface gives me the opportunity to express my sincere gratitude to some people. First and foremost, I wish to thank my supervisor, Professor Maud Piers, for endorsing an open door policy and for her invaluable comments, guidance, advice and editorial assistance in this endeavour. Many thanks as well to Pascal Hollander\textsuperscript{2} and Professor Eric De Brabandere\textsuperscript{3} for taking the time to shed some light on this utterly interesting subject during an interview. Furthermore, I wish to thank Professor Catherine A. Rogers for providing me a copy of a chapter in her forthcoming book,\textsuperscript{4} which has been extremely helpful in understanding some of the more cumbersome issues regarding the respective topic of this thesis.

Finally, I would like to express a special thank you to Sara, my parents, my brother and my friends who are very dear to me and who supported me, not only during the writing of this thesis, but also during the entirety of my education. I could not have written this thesis without them and am forever grateful for their kind understanding and moral support.

Ghent, 7 May 2014

Thibault De Boulle

\textsuperscript{2} Interview with Pascal Hollander on 15 April 2014.
\textsuperscript{3} Interview with Professor Eric De Brabandere on 23 April 2014.
## LIST OF ABBREVIATIONS USED

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<th>Abbreviation</th>
<th>Description</th>
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<tr>
<td>ABA</td>
<td>American Bar Association</td>
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<tr>
<td>ALF</td>
<td>Association of Litigation Funders of England and Wales</td>
</tr>
<tr>
<td>ATE</td>
<td>After-the-event</td>
</tr>
<tr>
<td>BTE</td>
<td>Before-the-event</td>
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<tr>
<td>CFA</td>
<td>Conditional fee agreement</td>
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<tr>
<td>IBA</td>
<td>International Bar Association</td>
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<tr>
<td>GDP</td>
<td>Great Britain Pound</td>
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<tr>
<td>ICC</td>
<td>International Chamber of Commerce</td>
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<td>ICDR</td>
<td>International Centre for Dispute Resolution</td>
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<tr>
<td>ILR</td>
<td>Institute for Legal Reform</td>
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<tr>
<td>LCIA</td>
<td>London Court of International Arbitration</td>
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<td>LEI</td>
<td>Legal expenses insurance</td>
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<td>LFA</td>
<td>Litigation funding agreement</td>
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<td>PCA</td>
<td>Permanent Court of Arbitration</td>
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<td>TPF</td>
<td>Third-party funding</td>
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<tr>
<td>U.K.</td>
<td>United Kingdom</td>
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<td>UNCITRAL</td>
<td>United Nations Commission on International Trade Law</td>
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<td>U.S.</td>
<td>United States</td>
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<td>USA</td>
<td>United States of America</td>
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<tr>
<td>USD</td>
<td>United States Dollar</td>
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<tr>
<td>USSC</td>
<td>Supreme Court of the United States</td>
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INTRODUCTION, SCOPE AND OBJECTIVES

1. TPF, which has existed in litigation in various forms and in several jurisdictions for quite some time, is now one of the ‘hot topics’ in international arbitration.\(^5\) The heretofore fledgling and virtually unknown phenomenon with only a few years of history is evolving into a veritable and thriving practice with each passing day. It is gradually gaining traction and credibility in the collective consciousness of the global legal community and it will inevitably become a feature of international commercial arbitration\(^6\) due to both the exponential growth of international investment and commercial disputes over the last fifty years and the rising costs associated with submitting a dispute to arbitration. This growth parallels the globalisation in international commerce, where international commercial arbitration is gradually becoming the most favoured method of resolving commercial disputes.

2. A considerable number of parties (referred to in industry jargon as “funded party”) in international arbitrations – whether engulfed by financial difficulties or otherwise\(^7\) – are now exploring the possibility of using TPF to provide the necessary capital to finance their meritorious claims, in return for a percentage of the compensation granted to the funded party if successful, whether by settlement or arbitral award. The financing of the costs associated with pursuing a claim by a third party – who only invests in the proceedings with the hopes of making a profit and has no interest in the substantive issues of the dispute, other than a pecuniary one – is becoming pivotal and indispensable for impecunious claimants and defendants to resolve their disputes with arbitration. In summary, international arbitration continues its dramatic growth on the one hand, and on the other hand, the ability to prosecute the arbitration claims is shrinking.

3. Notwithstanding the clear advantages of TPF, it is undeniable that TPF has its share of shortcomings and a lot of problematic issues remain open and are even growing. The key predicaments are the fact that the industry is virtually unregulated and that neither the funded parties, nor the third-party funders (“funder”)\(^8\) are subject to a mandatory disclosure obligation regarding the

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\(^5\) The author encourages readers to consult the following source, in which six short introductory films about TPF as such, and the ‘hot topics’ regarding TPF can be found. FOX WILLIAMS, Third Party Litigation Funding; The debate, 21 July 2011, [www.foxwilliams.com/news/230/](http://www.foxwilliams.com/news/230/).


\(^7\) Financially healthy companies may rely on TPF for reasons other than paucity of sufficient finances (infra 29-30, nos. 77-78).

\(^8\) Third-party funders have been referred to with different names, such as third party financiers, litigation funders, litigation financing entities, alternative dispute funders and third-party funders. A definitive name has thus not been agreed upon. The general terms of third-party funder and funder will be used throughout this thesis.
funding agreement, which can lead to numerous (sometimes detrimental) consequences. On the one hand, the rise of TPF is thus being lauded for increasing the access to justice for impecunious claimants; on the other hand, TPF is being vilified and decried for several reasons.

4. The first part of this thesis will engage in canvassing the framework of TPF by discussing and analysing different definitions and by comparing TPF to other funding mechanisms. Subsequently, after a brief history of TPF, this thesis will try to achieve a better understanding of the compelling reasons for the recent growth of this phenomenon. The second part of this thesis will be devoted to identifying and analysing the issues needing to be addressed in order to buttress the growth of TPF. The author acknowledges that many of the debates and discussions about TPF are based on empirical assumptions and predictions due to the scarcity of hard data to date.

5. Throughout this thesis several interesting cases will be highlighted in which the issue of TPF has been raised. The reader will notice that the majority of these cases are litigation and international investment arbitration cases. The rational and justification behind this is the simple fact that litigation is a type of dispute resolution that is significantly more public than international commercial arbitration. As for international investment arbitration, the majority of arbitral awards are published, whereas in international commercial arbitration, publication is still an exception.

6. Furthermore, it should be noted that the author will often rely on analogical reasoning with TPF in litigation and in international investment arbitration because a substantial body of case law and established practices concerning TPF has yet to develop in international commercial arbitration. Moreover, rules of confidentiality in arbitrations and confidentiality clauses in funding agreements make it onerous to discuss and examine TPF in international arbitration as such, which makes this phenomenon all the more opaque. Put differently in KANTOR’s words, even if there were precedents for TPF in international arbitration to date, “those precedents are themselves currently locked away behind bars of confidentiality.” Nevertheless, the principles and concepts of TPF remain mostly the same, regardless of the type of dispute resolution it is used in. Put differently, in the words of DUNN: “in terms of external funding, there is not much difference between litigation and arbitration.” Moreover, the way TPF is treated and regulated in litigation can prove to be crucial for international arbitral awards during proceedings to annul, vacate, enforce or recognize arbitral awards in state courts.

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10 S. DUNN, “Class of its Own”, 4(2) CDR 2010, 14.
7. This thesis’ predominant goal is to shed light on the reality of TPF and to create a reference source for students, academics and arbitration practitioners to whom the topic in question is relatively new, but also for those who are familiar with it and want to broaden their knowledge on the subject. The author acknowledges that TPF is most often seen on the claimant side – although TPF of respondents is also conceivable – and this thesis will therefore generally address the matter from their point of view. Moreover, as the title reads, the primary focus of this thesis is commercial claims and not claims such as human rights cases, class actions, and mass torts. Although TPF could also occur in the latter claims, it will not be subject to discussion in this thesis.

8. Furthermore, this thesis will concentrate on the leading jurisdictions for TPF at the moment, namely the United Kingdom (“U.K.”), the United States of America (“USA”) and Australia. The author acknowledges that there are other jurisdictions with a developed TPF industry, such as Germany, but due to a language barrier and space limitations, these jurisdictions will not be discussed in this thesis. The situation in Belgium will also not be discussed for the simple reason that the practice of TPF does not yet exist to any notable extent in this jurisdiction, nor has it been – to the best knowledge of the author – debated by the Bar, the Belgian legislature or any other Belgian organisation.

9. Finally, although the author assumes that the reader has a general understanding of international commercial arbitration, some terms will nevertheless be explained going along.

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11 See for instance Abaclat et al. v. Argentina Republic, ICSID Case No. ARB/07/05, 4 August 2011, in which the first ever mass claim in international investment arbitration was funded by a third party. For a discussion on this case, see A. Crivellaro, “Third-party funding and “mass” claims in investment arbitrations” in B. Cremades and A. Dimolitsa (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 137-141; see generally for a discussion of TPF in class actions, C. Veljanovski, “Third-Party Litigation Funding in Europe”, 8 J.L. Econ. & Pol’y 2012, 427-437.


FIRST PART – INTRODUCTION TO THIRD-PARTY FUNDING
CHAPTER I. DEFINING THIRD-PARTY FUNDING

10. Despite being one of the ‘hot topics’ in international arbitration, it is noteworthy that our view of TPF remains rather hazy. SCHERER put it correctly by saying that “the exact definition of third party funding, however, remains elusive and its legal and ethical implications in international arbitration, mostly unexplored.”

11. There is still no consensus on how this novel economic activity should be understood. Some qualify TPF as commercial lending contracts, while others consider it to be a form of insurance contracts. Accordingly, CREMADES states that “[t]he reasons why it is so difficult to reach a firm definition for litigation or arbitration funding derives from the many forms in which it manifests itself.” In view of the recent development of this burgeoning industry and with no straightforward answer in sight, definitions are still being created, adapted and becoming more established as time goes by.

12. The International Business Law Journal organised two roundtable discussions (“Roundtable Discussions”) on TPF. The delicate issue of defining TPF was, inter alia, keenly debated. The participants to the discussion did not, however, manage to reach a consensus regarding the definition of TPF.

13. The following section will discuss some of the proposed definitions and will identify the different types of TPF currently in existence.

1. Third-party funding sensu stricto

14. ENDICOTT, GIRALDO-CARRILLO and KALICKI’s definition is what this author considers to be TPF sensu stricto. They regard TPF as a financing method which involves the non-recourse funding of

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16 See e.g. C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, Ethics in International Arbitration, Oxford University Press, forthcoming June 2014; NEW YORK STATE BAR ASSOCIATION, Report on the Ethical Implications of Third-Party Litigation Funding, 16 April 2013, 1 and http://old.nysba.org/AM/Template.cfm?Section=Commercial_and_Federal_Litigation_Section_Reports&template=CM/ContentDisplay.cfm&ContentID=200115.
18 The Roundtable Discussions were held in Paris on 27 January 2012 and on 18 April 2012.
litigation or arbitration in return for a share of the proceeds by (bona fide)\textsuperscript{19} specialized providers who are neither parties to the dispute nor closely connected with it and whose sole interest is of a pecuniary nature.\textsuperscript{20} This type of financing will be envisaged throughout this thesis to identity TPF and to distinguish TPF from other types of funding relationships. In other words, TPF in this thesis should be read as TPF sensu stricto.

15. The quintessential scenario for TPF sensu stricto that predomnates in international arbitration is an arrangement between a client and an institutional funding corporation wherein it is agreed that the funder will cover a party’s legal costs and expenses of a legal claim\textsuperscript{21} in exchange for assigning to the funder a (often substantial) percentage of any proceeds deriving from the case. Hedge funds and other financial institutions can act as funders next to the institutional funders. However, this is most likely on a ‘one-off’ basis and this thesis will focus on institutional funders whose core business is TPF.

16. Ultimately, TPF sensu stricto is too narrow to capture the full range of relevant agreements, which is why TPF sensu lato will be discussed hereafter.

2. Third-party funding sensu lato

17. TPF sensu lato is but one source of financing available to a party. Other types of funding relationships often differ only in a subtle manner from TPF sensu stricto and can be qualified as TPF sensu lato. As said, this thesis’ primary focus is TPF sensu stricto. Nevertheless, in order to give the reader an understanding of the complexity and the multi-faceted character of TPF, it is worth discussing the many guises of TPF.

\textsuperscript{19}The possibility exists that the funder is not bona fide because it has other motives than pure financial gain, such as causing harm to the opposing (non-funded) party. See L. Lévy and R. Bonnan, “Third-party funding: Disclosure, joinder and impact on arbitral proceedings” in B. Cremaides and A. Dimolitsa (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 80.


\textsuperscript{21}These costs include legal fees, expert’s fees, arbitrator’s fees, registration fees to the administering institution and other institutional fees.
CHAPTER I. DEFINING THIRD-PARTY FUNDING

18. SCHERER defines TPF as “any financial solution offered to a party regarding the funding of proceedings in a given case.” It is clear that this definition includes several types of funding that are beyond the boundaries of TPF sensu stricto. Attorney financing, legal expenses insurance, loans, assignment of a claim, and donations are all financial solutions that can be obtained for the funding of a claim.

2.1. Attorney financing

19. Attorney financing is arguably the most obvious source of TPF since counsel can, in some jurisdictions, agree with their client that only a part of his or her usual fee, or no fee at all, will have to be paid during the arbitral proceedings, and that he or she will only be remunerated after and upon satisfactory closure of the case. This kind of financing of disputes is undeniably a type of TPF and therefore merits discussion in this thesis.

20. Three types of attorney financing can be identified and will be discussed separately: (i) pro bono legal representation; (ii) contingency fee arrangements; and (iii) conditional fee arrangements.

2.1.1. Pro bono

21. In brief, pro bono legal representation involves the attorney shouldering all costs related to representing his or her client, without a reasonable expectation of reimbursement. Pro bono legal representation is not regarded as a traditional type of TPF because the money does not usually change hands between the attorney and the client. However, in practice, the client may not experience a big difference with TPF because in both types of financing, the financial burden has been shifted from the client to a third party.

22. It should be noted, however, that it is highly unlikely that pro bono representation will play any role in international commercial arbitration because it is usually confined to criminal and civil actions. This explains the conciseness of the discussion on this topic. Still, the existence of it is worth mentioning to provide the reader a general overview of all the existent types of TPF and for the completeness of this thesis.

2.1.2. Contingency fee arrangements

23. Contingency fee arrangements can be defined as “any arrangement whereby the lawyer’s fee depends in whole or in part on the success of the claim.” Working on a contingency basis thus means that if there is no recovery, then the lawyer does not receive any fee and the practical consequence of this is pro bono representation. Conversely, if there is recovery, then the lawyer’s legal services will be repaid along with a handsome additional fee based on a percentage or fraction of the amount recovered. Similarly to pro bono legal representation, the lawyer assumes the financial risks. Accordingly, “these arrangements are only entered into by lawyers where a claim is considered to be sufficiently strong and a sufficient recovery is contemplated to offset the risk to the lawyer of non-payment.”

24. Contingency fee agreements are common practice in the USA. In contrast, English law traditionally imposed particularly stringent prohibitions on contingency fee arrangements. In Bevan Ashford v. Geoff Yeandle, Vice-Chancellor SCOTT expressly held that the prohibition on contingency fees extended to arbitrations, and dismissed earlier suggestions from Lord Justice STEYN in Giles v. Thompson that, because arbitration was a consensual process, the same public policy objections based on the tort of champerty might not apply. However, since 1 April 2013, contingency fee agreements can now also be used in civil litigation in the U.K. Nevertheless, as the use of TPF continues to expand, further debate and developments are inevitable regarding the scope and effect of contingency fee arrangements in international arbitrations when England is the venue for the proceedings.

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27 With respect to the additional fee, the attentive reader can notice a clear parallel with TPF.
29 The United States Supreme Court (“USSC”) confirmed the legality of contingency fee agreements in Stanton v. Embrey, 93 U.S. 548 (1877), p. 556.
32 Infra 40-47, nos. 95-118.
34 Art. 45 Legal Aid, Sentencing and Punishment of Offenders Act 2012.
25. Finally, it should be noted that contingency fee arrangements are still prohibited in numerous jurisdictions, such as France and Belgium.

2.1.3. Conditional fee arrangements

26. Conditional fee arrangements (“CFA”) are similar to contingency fees, with the exception that the client has to pay a discounted fee – in lieu of no fee – unless the client wins. In other words, the attorney carries the entirety of the risk of loss in contingency fee arrangements, whereas the risk is divided in CFAs, thus ensuring the attorney to receive at least partial remuneration. If the claim is successful, the lawyer is then paid his or her usual fee plus an uplift or ‘success fee’.

27. CFAs are allowed and commonly used for funding in civil litigation in England. There are some English solicitors who are working with CFA in arbitrations. CFAs – as in arrangements where an additional fee is paid in the event a successful outcome of the proceedings is achieved – are also permitted in several jurisdictions such as France and Belgium.

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40 See section 58A of the Courts and Legal Services Act 1990, which stipulates that CFAs may be made in relation to proceedings, which are defined to include “any sort of proceedings for resolving disputes”. Hence, CFAs are also possible in arbitration.

41 Remember the difference with ‘pure’ contingency fee arrangements whereby a lawyer is only remunerated on the basis of a proportion of the amount recovered.

CHAPTER I. DEFINING THIRD-PARTY FUNDING

2.1.4. Applicability to arbitration of the prohibitions against attorney financing

28. The national rules prohibiting certain forms of attorney financing are clearly intended to apply to domestic litigation. One might legitimately wonder whether these rules also apply to international arbitration.

29. To date, no straightforward answer can be reliably offered with regard to the question at hand. No uniform application of the prohibitions against attorney financing in international arbitration can be discerned prima facie. This issue demands an extensive comparative analysis of the respective national rules and this is not within the ambit of this thesis. Nevertheless, the author encourages commentators and scholars to explore and analyse this delicate issue in order to impart on attorneys more knowledge regarding the question whether, and to what extend, attorney financing is permitted in international arbitration.

2.1.5. Relationship with third-party funding sensu stricto

30. Prima facie, contingency fee arrangements are similar to TPF with the exception that in TPF the funder is an outside entity, rather than the client’s attorney or law firm. Furthermore, where lawyers are subject to mandatory ethics rules and bar associations, TPF is still mainly unregulated. The funder has more freedom to determine his financial commitment and has the opportunity to be involved in the management of the case. Additionally, the funder can weigh in on the choice of counsel, whereas in contingency fee agreement, the choice of counsel is by definition predetermined. Another key difference is the fact that the financing is provided by a party (i.e. the lawyer) already involved in the arbitration. TPF on the other hand, adds a new party (i.e. the funder) to the proceedings. Finally, whereas TPF requires the investment of third-party capital as such, contingency fee arrangements require lawyers to invest his or her professional services and time in lieu of capital.

43 In France, for instance, the Paris Court of Appeal ascertained that pure contingency fee agreements were possible in international arbitration – despite being invalid in principle – because such agreements were widely recognized as valid in international commerce. See Court of Appeal of Paris 10 July 1992, Rec. Dalloz 1992, 459, note J. CHARLES; Rev. Arb. 1992, 609; as for Switzerland – where contingency fee agreements are also invalid in principle – it appears that the prohibition also applies to Swiss lawyers in international arbitration. See D. WEHRLI, “Contingency Fees / Pactum de Palmario “Civil Law Approach””, 26(2) ASA Bulletin 2008, 250.
44 infra 94-97, nos. 259-267.
45 infra 55-57, nos. 143-146.
31. Many law firms are usually reluctant to discuss sizeable contingency fee arrangements because it involves an almost undue degree of risk, which law firms try to avoid risk as much as possible, especially now in the current economic turbulence. Law firms unwilling to undertake contingency work can only serve solvable clients who can afford their fees. Law firms therefore welcome TPF because it means payment of their fees on a regular basis. The client will notice only a modicum of difference between TPF and contingency fee arrangements in practice because in both cases he or she will not, or only partially, have to pay in case of a less than favourable outcome of the claim.

32. Furthermore, contingency arrangements or CFA are only partial solutions to the problem because they only cover the legal fees and not for instance the arbitrators’ fees. Therefore, contingency arrangements and CFA every so often collaborate with funders to share the risk. However, it appears that most funders are not fond of lawyers becoming co-funders, especially considering that they have already taken a very large part in the financing of the case.

2.2. Legal expenses insurance

2.2.1. General

33. Legal expenses insurance (“LEI”) is one of the most common types of TPF and is used to cover the financial risks associated with a lawsuit. LEI policies will cover the legal representation or will pay any award or judgement against the insured party, or sometimes even both. The key feature of LEI is that the insurance policies often contain provisions transferring a significant amount of control over the case from the claimholder to the insurance company. For instance, the insurance company may have discretion to decide how vigorously and zealously they should pursue the case and when to settle. This feature is also what separates LEI from attorney financing from the client’s point

of view, because the client retains control over the management of the dispute in all three types of attorney financing.  

### 2.2.2. Specialized forms of insurance

34. Besides the traditional LEI policies, there are also specialized forms of insurance that can be purchased either before or after the occurrence of an incident that gives rise to a dispute, namely ‘after-the-event’ (“ATE”) insurance and ‘before-the-event’ (“BTE”) insurance. BTE and ATE insurance are thus taken out before or after an event has occurred, such as an accident or a contractual dispute, to protect the insured party against the non-negligible risk of having to pay the other parties (often hefty) costs in the event that party loses in subsequent litigation of arbitration or to cover the policyholder’s own ‘out-of-pocket’ disbursements, or both. If the policyholder succeeds in the litigation or arbitration, a premium will then have to be paid to the insurer.

35. The difference between these specialized types of insurance and the traditional LEI is that the specialized insurance policies will cover the attorney fees and other expenses, without taking full control over the proceedings and it will not cover the payment of awards or judgments, which is most often the case in LEI. Therefore, ATE and BTE insurance policies customarily do not require the insured party to transfer most of the control of the case to the insurer.

### 2.2.3. Relationship with third-party funding sensu stricto

36. In practice, TPF and ATE insurance have a lot of similarities. Both are interested in determining the chance of success of a claim, and both have access to capital, which they can advance to support the claim. There is nonetheless a fundamental conceptual difference, namely the investment aspect, which TPF has and ATE does not. Nevertheless, it is not uncommon for insurers to work in partnership with funders and it is likely that this will continue to grow.

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54 Supra 7-9, nos. 19-27.
CHAPTER I. DEFINING THIRD-PARTY FUNDING

37. The nature of the return further differentiates TPF and insurance contracts since the return to the funder is usually either a percentage of the recovery or a multiple of the capital invested, whereas in insurance contracts, the insurer is paid a premium.

2.3. Loans

38. Loans in the context of the financing of claims are typically obtained from the client’s attorney or law firm or from a traditional bank or other financial institution to finance (usually rather small) claims in exchange for a share of a favourable outcome. The key difference with TPF sensu stricto is the fact that loans must be repaid regardless of the outcome of the dispute. AFFAKI also notes that “funds offer much more in terms of bundled claim management services than the mere supply of money and, consequently, are not in direct competition with banks in the lending business.” Furthermore, “funding companies do not typically charge interest, but instead they secure a percentage of the recovery at different levels to be paid according to varying timeframes.”

39. The primary advantage of this type of TPF is that the client retains complete control over the management of the dispute. The obvious disadvantage of loans is that the client cannot alleviate the risks of losing the case because the client has to repay the lender regardless of the outcome of the dispute.

40. Despite the – in the author’s view – evident discrepancy between TPF sensu stricto and loans, TPF is occasionally qualified as loans. For instance in the U.S., recently introduced legislation calls the product of lawsuit funding loans.

59 The NEW YORK STATE BAR ASSOCIATION states that most loans (or cash advances as they call it) only consist of a few thousand USD. See NEW YORK STATE BAR ASSOCIATION, Report on the Ethical Implications of Third-Party Litigation Funding, 16 April 2013, 1 and http://old.nysba.org/AM/Template.cfm?Section=Commercial_and_Federal_Litigation_Section_Reports&template=/CM/ContentDisplay.cfm&ContentID=200115; conversely, the TPF sensu stricto market is so lucrative due to generally large claims involved.


2.4. Assignment of a claim

41. An assignment of a claim may occur for numerous reasons, such as mergers and acquisitions and liquidation following bankruptcy. By assigning a claim, the party loses full control over the management of the lawsuit, including the power to settle and the power to choose attorneys. Additionally, the funder (i.e. the assignee) will become a party in the arbitration. CREMADES explains the difference between assignment of a claim and TPF:

“[W]hereas in the assignment of lawsuits the litigant sells the lawsuit itself, in third party funding the litigant merely sells the possible “fruits” of the lawsuit.”

42. In TPF, the client does in fact assign a share of the proceeds of the successful claim to the funder in lieu of assigning the right to pursue the claim. The main difference is thus that assigning a claim involves the sale of the claim, whereas in TPF, the claim remains entirely with the original creditor. However, it is likely that the funder will exercise some, if not a substantial amount, of influence on the lawsuit. For this reason, it can be onerous to distinguish in practice between TPF and assignments of claims from a client’s point of view if we use the criteria of exerting control over the lawsuit to make the distinction.

43. SEBOK states that the funder is an assignee and that the contract between the funder and the funded party should be a contract in assignment if the funder assumes full control of the lawsuit. However, the author opines it to be unlikely that a funder will have full control. Nevertheless, one should be cautious when qualifying a funding agreement as either a TPF or an assignment of claim.

66 Infra 55-57, nos. 143-146.
68 As will be explained in a later paragraph (infra 40-47, nos. 95-118), the doctrines of maintenance and champerty could object to a full control of the funder. Furthermore, the funder does not want to become a party in the arbitration by exercising too much control because this can have several detrimental consequences, such as liability for adverse costs awards (infra 73-80, nos. 194-212).
2.5. Donations or free financial assistance

Besides the traditional scheme of a funder who funds the arbitral proceedings with financial gain on its mind, there are also international arbitrations where the proceedings are funded by a third party, who provides the financing for reasons other than making a profit since the funded party can keep the financing, regardless of the outcome of the proceeding. These instances can be qualified as donations rather than funding agreements. A vivid example is the ICSID case of Philipp Morris v. Uruguay, where the peculiarity was that the “Campaign for Tobacco-Free Kids” supported the Uruguayan Government financially out of pure altruistic motivation because it undertook to bear the costs without demanding a piece of the proceeds expected from the award.69

2.6. Conclusion

While there are already various funding options for international arbitration claims, there is nevertheless still a need for TPF. The large financial benefits and risks associated with arbitration claims provide for attractive opportunities for funders in the future and accordingly will constitute a valuable resource for claimants.

As it was argued, the different funding arrangements might have the same results in practice. The key difference between TPF and any of the above-mentioned funding arrangements is most often of a conceptual nature. TPF is undeniably an investment, whereas the other funding arrangements have different objectives.

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CHAPTER II. IDENTIFICATION OF INDUSTRY PARTICIPANTS

1. Potential clients

47. There are different types of potential clients who could need outside funding at some point to finance the litigation or arbitration in which they are involved: (i) individuals; (ii) law firms and corporations; and (iii) even sovereign states. Although the literature on TPF focuses almost exclusively on the funding of claimants when discussing potential clients, defendants can use TPF just as well. A financially constrained or risk-averse defendant equally deserves adequate funding protection. The traditional situation where a defendant may seek TPF is when a counter-claim is filed by him or her.

48. However, the availability of TPF is not always well-known, which is deleterious to the industry because the industry appears to exclusively promote claimants’ claims and it could be portrayed as a tool designed to abuse defendants. No doubt that it will take some time for defendant funding to develop. During the Roundtable Discussions, the participants concluded that there is a clear demand for defendant funding. However, it should be noted that none of the participating funders in attendance had funded such cases prior to the Roundtable Discussions.

49. With respect to international investment arbitration, it should be noted that sovereign states are also increasingly being funded by third parties, thus making TPF not a mechanism exclusively relied upon by private entities.

70 For a concise overview of the funding options for defendants, see B. CREMADES, “Third party litigation funding: investing in arbitration”, 8(4) TDM 2011, 16-25 and www.curtis.com/siteFiles/Publications/TDM.pdf.

2. Potential funders

50. The most common funding entities are: (i) the client’s attorney or law firm (where authorized); (ii) insurance companies; (iii) institutional funders, such as Juridica Investments (U.K.), Burford Capital (U.S.), Calunius Capital (U.K.), Fulbrook Management (U.S.), Omni Bridgeway (NL), and Harbour Litigation Funding (U.K.); (iv) or other financial institutions, such as corporations, banks and hedge funds.74

51. Some financial institutions indeed offer TPF, but ordinarily on a ‘one-off’ basis and this activity is only a part of their wide offer of traditional financial investments. Furthermore, there are also institutional funders that are specialized in TPF and whose sole business activity is the funding of arbitration and litigation claims. It is rather self-evident that the majority of specialized institutional funders are based in jurisdictions with an established or rapidly developing TPF industry (i.e. Australia, the U.S., and the U.K.).


CHAPTER III. HISTORY

52. In brief, the TPF industry in international arbitration is still relatively young, with only few facts and figures available as to the extent of its use. The following paragraphs will discuss the history of TPF in litigation and international arbitration separately because of the different evolutions TPF has experienced in the respective industries.

1. Growth in the use of third-party funding in domestic litigation

53. In the litigation context, a clear shift in judicial attitude can be observed from being reluctant to accept TPF, to the current situation where many jurisdictions have a relaxed attitude towards TPF. The future growth and further development of the TPF industry will depend on the direction of the jurisprudence in the jurisdictions with a developed TPF industry, as well as in jurisdictions where TPF is beginning to manifest itself. The jurisprudence in question is mostly related to the funders’ and attorneys’ professional and ethical responsibilities and the legal doctrines (i.e. maintenance, champerty, and usury) prohibiting TPF agreements. TPF is now widely seen as an essential means of facilitating access to justice for claimants who have meritorious claims but are incapable to finance litigation. TPF is most commonly used in Australia, England and the USA. Australia has the largest TPF industry and it is believed that the

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55. Infra 40-47, nos. 95-118.
58. It appears that most commentators stipulate these three jurisdictions as the leading jurisdictions. See e.g. C. BURKE ROBERTSON, “The Impact of Third-Party Financing on Transnational Litigation”, 44. Case W. Res. J.
TPF industry was born approximately 25 years ago in this jurisdiction,\(^8^3\) where it is now an established part of the civil justice system.\(^8^4\) England now has a TPF industry, which is only closely behind Australia in its ample use of TPF.\(^8^5\) As for the U.S., the TPF industry is slowly developing since the early 1990s, but is still lagging behind those in Australia and the U.K.\(^8^6\) A possible explanation is the


\(^8^3\) In Australia, one of the possible explanations for the development of TPF is the fact that contingency fee arrangements are prohibited. Therefore, there was a need for another type of funding to cover the legal expenses and this is where TPF made his grand entrance. See U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States, October 2009, 9 and http://legaltimes.typepad.com/files/thirdpartylitigationfinancing.pdf; S. SEIDEL, “Investing in Commercial Claims, Nutshell Primer”, Fulbrook Management LLC Publications 2011, 3 and http://fulbrookmanagement.com/publications/Nutshell-Primer.pdf; S. SEIDEL and S. SHERMAN, “Corporate governance” rules are coming to third party financing of international arbitration (and in general) in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 35.


fact that contingency fees\textsuperscript{87} and other payment schemes were first permitted in the USA. Hence, there was less need for TPF.\textsuperscript{88} However, the industry is now garnering attention,\textsuperscript{89} with companies continuing to enter the U.S. market. Given the exponential growth of TPF in domestic litigation, especially in these three jurisdictions, it is very probable that such funding will surge in international commercial arbitration as well.

55. In Europe,\textsuperscript{90} although Germany\textsuperscript{91} and Switzerland\textsuperscript{92} have developed a sound TPF market, TPF is nonetheless nearly non-existent in other civil law nations.\textsuperscript{93} The absence of TPF in civil law countries can be explained by a number of reasons, such as costs and procedural rules, a less litigious culture, and the traditionally more personal nature of a claim.\textsuperscript{94} If the TPF industry continues to grow in other jurisdictions, and the benefits of this funding becomes clear, together with the skyrocketing litigation costs, it is likely that the TPF industry will also grow in civil law countries.\textsuperscript{95}

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\textsuperscript{87} Supra 8-9, nos. 8-9.


\textsuperscript{89} For instance, the American Bar Association (“ABA”) is now paying more attention to issues that third-party litigation funding could entail, such as the influence of a funding relationship on the attorney-client relationship and on the ethical and professional duties of attorneys. See e.g. AMERICAN BAR ASSOCIATION COMMISSION ON ETHICS 20/20, Informational Report to the House of Delegates, February 2012, www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_bod_informational_report_authcheckdam.pdf.

\textsuperscript{90} There is currently no legislation in Europe that specifically addresses TPF. See M. SCHERER, A. GOLDSMITH and C. FLÉCHET, “Le financement par les tiers des procédures d’arbitrage international – une vue d’Europe Seconde partie: le debat juridique / Third Party Funding of International Arbitration Proceedings – A view from Europe Part II: The Legal Debate”, RDAI/IBLJ 2012, 654.


\textsuperscript{92} In Switzerland, a draft of a statute to prohibit litigation funding was declared invalid by the Federal Supreme Court on 10 December 2004 because it was contrary to the Constitutional principle of freedom of commerce. See Decision of the Federal Supreme Court, Dec. 10, 2004, FTD 131 I 223 (Switz.) (interpreting art. 27 of the Federal Constitution of the Swiss Confederation of 18 Apr. 1999, Sr 101).


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\textsuperscript{97} http://old.nysba.org/AM/Template.cfm?Section=Commercial_and_Federal_Litigation_Section_Reports&template=CM/ContentDisplay.cfm&ContentID=200115.

\textsuperscript{98} See supra, 9, nos. 8-9.


\textsuperscript{100} For instance, the American Bar Association (“ABA”) is now paying more attention to issues that third-party litigation funding could entail, such as the influence of a funding relationship on the attorney-client relationship and on the ethical and professional duties of attorneys. See e.g. AMERICAN BAR ASSOCIATION COMMISSION ON ETHICS 20/20, Informational Report to the House of Delegates, February 2012, www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_bod_informational_report_authcheckdam.pdf.

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\textsuperscript{103} In Switzerland, a draft of a statute to prohibit litigation funding was declared invalid by the Federal Supreme Court on 10 December 2004 because it was contrary to the Constitutional principle of freedom of commerce. See Decision of the Federal Supreme Court, Dec. 10, 2004, FTD 131 I 223 (Switz.) (interpreting art. 27 of the Federal Constitution of the Swiss Confederation of 18 Apr. 1999, Sr 101).


2. Availability of third-party funding in international commercial and investment arbitration

56. TPF in international arbitration is still in its infancy in both international investment arbitration and international commercial arbitration. It is considered new, not in the sense that a new financing method was invented, but in the sense that an already existing method is now being used in another industry than litigation. TPF in arbitration is in many ways very similar to TPF in litigation. Nonetheless, due to the nature of arbitral proceedings, there are some subtle nuances that need to be identified and analysed.

57. As for international commercial arbitration, despite the paucity of available hard data due to the private, secretive and often confidential nature of the proceedings, one can notice several indications and anecdotal evidence that denote an exponential growth of the demand for TPF services. First, the subject has caught the eye and pen of the news media, academics and scholars in recent years, which explains the burgeoning of the literature on this topic. Furthermore, in the wake of this increased attention, conferences have recently been organized solely around TPF in international arbitration. A vivid example of the enhanced attention for TPF in international arbitration is the recently launched “Third-Party Funding Taskforce”, which is organized by the International Council for Commercial Arbitration in collaboration with the Centre on Regulation, Ethics and Rule of Law at Queen Mary, University of London. This taskforce will study and table recommendations regarding the procedures, ethics and related policy issues relating to TPF in international arbitration.

58. Second, as already noted above, TPF is thriving in domestic litigation and the skills and experience developed in this area will inevitably amount to an exponential growth of TPF in international arbitration.

59. Third, the increase of the volume of disputes resolved in arbitration, the escalating costs incurred during these proceedings, the rapid professionalization of arbitration finance as an asset class,

97 For example, see the “32nd Annual Meeting of the ICC Institute of World Business Law: Third Party Funding in International Arbitration” organised on 26 November 2012 and the above-mentioned Roundtable Discussions (supra 5, no. 12); another conference was organized by the New York State Bar Association and Fordham University School of Law on 15 June 2011, titled the “Roundtable on Third Party Funding of International Arbitration Claims: The Newest “New New Thing”.
98 For further information on this taskforce, see www.arbitration-icc.org/projects/Third_Party_Funding.html.
99 Supra 18-20, nos. 53-55.
100 International commercial arbitration is now used throughout the world, with thousands of cases being administered by arbitral institutions, such as the International Chamber of Commerce (“ICC”), the International Centre for Dispute Resolution (“ICDR”) and the London Court of International Arbitration (“LCIA”). The following are some recent statistics in order to impart on the reader an idea of the magnitude of the international
and the fact that specialist funders are explicitly stating in marketing materials that they offer funding for international arbitration as well, are all factors that point towards the likely use of TPF.

60. Some specialized funding corporations are thus now making their services available to international arbitration claims. Due to this professionalization, funders have acquired a high degree of expertise on the subject, resulting in a more efficient process, a better assessment of risk, and a better understanding of pricing. All of these elements understandably increased the number of parties seeking to use this type of financing.

61. Finally, the lucrative business of TPF has been used and questions have been raised in international investment arbitration, where – in contrast to commercial arbitration – the awards are generally publicly available. This evolution can be considered an indication of the probable use of TPF in the more confidential industry of international commercial arbitration. This also explains why this thesis will discuss some international investment arbitral awards.

62. Nevertheless, despite the extensive press coverage of this rapidly emerging practice and the recent attention it enjoyed from academia, TPF remains a subject of some mystery. The knowledge vacuum is considered to be the industry’s biggest enemy because it negatively impacts the acceptance and growth of the industry.

arbitration business. First, the ICC registered an average of approximately 800 requests for arbitration per year from 2009 through 2012 (available at www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Introduction-to-ICC-Arbitration/Statistics/). Second, the ICDR grew rapidly over the past six years; 621 cases were administered in 2007, increasing to an impressive 996 cases in 2012 (available at www.adr.org/cs/idcplg?IdcService=GET_FILE&dDocName=ADRSTAGE2015007&RevisionSelectionMethod=LATESTReleased).


Supra 17, no. 50.


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63. To date, arbitration practitioners and parties to arbitral procedures only have a modicum of knowledge about TPF and some are even suspicious of it. This can be explained by the historical prohibition against stranger funding under the common law doctrines of maintenance and champerty. These doctrines made financial support of litigation by a third party a crime and a tort in certain jurisdictions. The effect of these doctrines has been relaxed over the past couple of years in some jurisdictions by the deterioration of the laws against these doctrines. This topic will be discussed in detail in a further subsection.

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110 Infra 40-47, nos. 95-118.
CHAPTER IV. WHY THIRD-PARTY FUNDING?

1. General

64. In international arbitration, party autonomy is a sacrosanct principle and it allows parties to determine how the proceedings are to be conducted, subject to mandatory rules of jurisdiction and, if applicable, to arbitral institution rules. TPF of arbitration claims is therefore, in principle, often allowed. The attention given to TPF in recent years can be explained by some fundamental advantages that TPF entails. Both claimants and respondents can take the advantage of TPF during the entire length of the proceedings and beyond (i.e. at the stage of the enforcement of the arbitral award).

65. One of the key issues that feeds the suspicion and scepticism of TPF is the fact that a stranger to the attorney-client relationship is introduced in the proceedings, whose sole interest in and connection with the dispute is a capitalistic aim of making a profit. This scepticism contributes to the not so flattering names – given by fierce detractors of TPF – by which funders are occasionally described: vulture investors, gamblers, or even loan sharks. WENDEL goes even further by saying that TPF is “objectionable in the same way as prostitution, selling babies, surrogate pregnancy, or establishing a market mechanism for the allocation of blood or organs for transplantation is potentially believed to be – namely, some things just should not be for sale.” PARLOFF states – in a slightly less dramatic fashion – that “there’s something about all this secret meddling in other people’s bitterest disputes and profiting from them that doesn’t sit well.”

66. In the following paragraphs, the main advantages of TPF will be discussed as well as some of the vices and reasons why TPF should be restricted or even prohibited.

2. Access to justice

2.1. General

67. The first and perhaps foremost reason for the expansion is that TPF is considered a solution for realising the public policy ideal of increasing access to justice. As a result from the financing, parties can have a realistic chance of vindicating their rights by having the opportunity to go to arbitration, without the risk of being pushed into economic dire straits by pursuing the claim. In other words, TPF levels the playing field by which disputes are resolved. The lack of access to justice could also affect the perceptions about the fairness and legitimacy of international arbitration as such. The latter is a non-negligible risk that the international arbitration community most definitely should try to avoid.

68. Open and equal access to arbitration for parties who want to make use of it, is a fundamental characteristic of any meaningful system. The author shares the opinion of DE BRABANDERE and LEPELTAK when they state that the increase of the access to justice is the most prevalent advantage of TPF. This incisive motive should be the backbone of the drive for further development of TPF.

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69. Some arbitral proceedings are a contest of equals if the companies are tantamount with respect to their size and the amount at stake is manageable for both parties. In that event, one would expect the dispute to be resolved based purely on its merits and not because one of the parties has a larger bargaining power. Conversely, the problems occur if one of the parties is much smaller than the other. Increasing expenses associated with the pursuit of high value claims and the need to manage the financial risks relating to the pursuit of these substantial claims certainly are a couple of reasons that can explain the rising interest in demand for TPF.124

70. Arbitration has become a great international industry, enormously competitive and also prohibitively expensive with the level of costs continuing to rise at an unsustainable rate,125 resulting in bargaining imbalances if one of the parties is significantly larger than the other, which makes arbitration a type of dispute resolution with an enormous demand for funding. The author asserts that justice should not only be available for ‘deep-pocket’ companies, but also for smaller companies that have a meritorious claim or a solid defense but are too wealth-constrained to go to arbitration. This will not only benefit the smaller enterprises, but might also boost the public opinion about the legal system as such. Wealth should not have, as BENTHAM so rightly stated, “the monopoly of justice against poverty.”126 A legal system “that inadequately imposes the costs of wrongdoing and contract-breaking on the parties who can best avoid them” should thus be avoided.127

71. The following examples are two recent cases in which it is determined that TPF is more and more an accepted tool to enhance the access to justice. The cases relate to the access to the civil courts and not to arbitration. The same principles nevertheless apply and are therefore relevant for arbitration as well. The first case is the English Court of Appeal decision of Arkin v. Borchard Lines (“Arkin”). In this case the court acknowledged that TPF could indeed offer access to justice. In their judgment, the Court referred to commercial funders as funders “who provide help to those seeking access to justice


125 Some commentators are expressly stating that the issue of the rising costs of arbitration should be addressed because it could damage the world of arbitration as such. See e.g. S. MENON, “Some Cautionary Notes for an Age of Opportunity”, Chartered Institute of Arbitrators International Arbitration Conference 22 August 2013, 10 and www.singaporelaw.sg/sglaw/images/media/130822%20Some%20cautionary%20notes%20for%20an%20age%20of%20opportunity.pdf.


which they could not otherwise afford.” A similar opinion was expressed by Justice Kirby in the Australian High Court case of Campbells Cash and Carry Pty v. Fostif Pty (“Fostif”). Justice Kirby expressly emphasized “the importance of access to justice, as a fundamental human right which ought to be readily available to all.” Furthermore, Lord Justice Jackson, in his published report of his review of the costs of civil litigation in England, concluded that TPF promotes access to justice.

72. No longer is international arbitration the prerogative of large multinationals because of TPF. Small and medium-sized companies exercising their rights through arbitration claims is becoming increasingly common, which can only be applauded and encouraged.

2.2. Impact on settlements

73. One of the key concerns with arbitrations where the opposing parties are unequal in size, is that the weaker of the two parties would be tempted to accept a ‘less-than-reasonable’ settlement offer that would free the party of the burdens of ongoing dispute resolution, regardless of the strength of its claim. Without a credible threat of taking the case through arbitration and potential enforcement proceedings, the weaker of the parties will thus usually have to settle with a one-sided settlement agreement. In this respect, TPF can have a ‘bargaining-power-equalizing’ function.

74. Proponents of TPF assert that TPF will have a positive impact on settlements and could prompt early settlements because of two reasons in particular: (i) the financially stronger party will lose the power to impose one-sided settlement agreements; and (ii) the presence of a funder is an indication to the opposing party that the claimant has a strong case and this increased leverage of the funded party will give the opposing party a bigger incentive to negotiate a more favourable

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129 Campbells Cash and Carry Pty Ltd. v. Fostif Pty Ltd. [2006] HCA 41; the High Court of Australia confirmed in this case that it is not contrary to public policy under Australian law for a funder to finance and control litigation in the expectation of profit, nor that this amounts to an abuse of the court’s process. See also W. Attilill, “Ethical Issues in Litigation Funding”, IMF 16 February 2009, 3-7 and www.imf.com.au/pdf/Ethical%20Issues%20Paper%20IMF09%20-%20Globalaw%20Conference.pdf for a discussion on this case.


settlement. Additionally, the fact that funding agreements are often structured as to favour an early settlement by providing that a smaller amount will be charged if the case is settled at an earlier stage also contributes to the positive effect TPF has on settlements. 

75. Conversely, detractors of TPF argue that TPF could have a negative impact on settlements because a rational claimant would be reluctant to settle for any amount that is less than the amount advanced by the funder. Accordingly, the presence of TPF disincentives funded claimants to settle. By the same token, funders will supposedly be reluctant to accept settlement offers that do not reimburse their complete investment. However, BOGART argues that “there is no evidence to suggest that claimants hold out for higher settlements because they need to pay the funder something, any more than there is evidence of claimants wanting higher settlements to cover the bank interest they have had to pay to borrow money for their legal fees.” BOGART makes the following analogy to prove his point. He says that plaintiffs in the USA commence litigation with lawyers who offer contingency fees. By entering into a contingency fee arrangement, the plaintiffs are aware that they are giving up a share of a potential settlement. However, these plaintiffs accept this from the outset and there are no reasons to suggest that plaintiffs would not agree with a reasonable settlement offer due to the presence of the contingency fee. TPF in arbitration is arguably no different.

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134 For example, in 2009, Burford Capital Limited agreed to fund Gray Development Group and in the funding agreement it was determined that Burford would advance USD 5 million in exchange for 33% of any settlement and 40% of any judgment. In other words, Gray Development Group had to pay 1/3 of any settlement. See B. CREMades, “Third party litigation funding: investing in arbitration”, 8(4) TDM 2011, 14 and www.curtis.com/siteFiles/Publications/TDM.pdf; see in the same sense the Anglo-Dutch Petroleum v. Haskell, 193 S.W.3d 87 (Tex. 2006), 105 case where the Texas Court of Appeals noted: “because of the increasing returns to which appellees were entitled, the manner in which the agreements were structured may actually have encouraged settlement.”


138 Ibid.
Both the proponents and the detractors of TPF thus cite the industry’s effect on settlements as support for their respective positions and both bring legitimate arguments. The author, however, tends to give more weight to the view of the proponents, simply because of the effect TPF has, or could have, on bargaining imbalances.

3. Maintain financial stability

The possible impact on the economic and financial viability and stability of the company can also discourage a party to submit its dispute to arbitration. TPF shifts the liability for the costs to the funder, thereby giving more companies the opportunity to engage in an arbitral procedure and securing companies to maintain enough cash flow and avoid liquidity or financial problems so they can continue their usual business or even invest in new business activities when they are pursuing a meritorious claim. Companies might withdraw from arbitral procedures if they risk a cash drain when they would continue the procedures. At that point, they are making a balance of what would engender the most damage; the cash flow issues with resulting stagnation of their business or withdrawing their claim and stop the arbitral procedure. TPF can be a solution to this dilemma because it allows the party to offload the financial risk and cost of the proceedings off their balance sheets by transferring the risks to the funder, while still having the opportunity to continue their usual business.

The concern in many arbitral procedures is that if the claim fails, the claimant will be liable for not only its own legal fees and expenses, but also for the respondent’s costs. The ability to spread the risks and benefits of third party funding is a panacea or a plague? A discussion of the risks and benefits of third party funding”, 8(4) TDM 2011, 4 and www.imf.com.au/docs/default-source/site-documents/tdm_tpf_oct2011; S. SEIDEL and S. SHERMAN, “‘Corporate governance’ rules are coming to third party financing of international arbitration (and in general)” in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 35.


This will depend on whether the applicable lex loci arbitri contains provisions under which the winner is usually entitled to recover its costs from the loser, unless the parties have agreed otherwise. Alternatively, where
and share these financial risks with a third party may be attractive, even to clients with strong businesses and cash flows.

4. Attractive investment from a funder’s perspective

79. From a funder’s perspective, TPF in international arbitration has an almost irresistible allure due to myriad reasons: (i) the speed of arbitral proceedings; (ii) the high enforceability of arbitral awards because of many treaties providing for international enforcement, such as the New York Convention; \(^{143}\) (iii) the prevalence of high-value claims; (iv) the expertise of the decision-makers; (v) the fact that funders usually seek a share of the recovery which oscillates between 15% and 50%, depending on the costs and risks associated with the funding of the dispute; \(^{144}\) and (vi) the stagnation of the worldwide economy and the accompanying uncertainty causes funders to have an amplified interest in TPF because they consider TPF as a way to make investments that are unrelated to the unpredictable financial markets. \(^{145}\)

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\(^{143}\) The New York Convention 1958 governs the recognition and enforcement of foreign awards. There are currently 147 countries that have signed the New York Convention. For an up-to-date list of the signatories countries of the New York Convention, see [www.newyorkconvention.org/contracting-states/list-of-contracting-states](http://www.newyorkconvention.org/contracting-states/list-of-contracting-states).


CHAPTER IV. WHY THIRD-PARTY FUNDING?

5. Assessment of the merits of a claim

80. Furthermore, another reason for choosing TPF is the early, independent, and fine-tuned assessment of the merits of a potential claim that one receives when contacting a funder. Once the funder received the request, the common modus operandi is to subsequently perform a proper and meticulous due diligence analysis in order to better assess the possibilities of success or the likelihood of failure. The requesting party will subsequently have an indication of the strength of its claim or defense due to the ability of funders to engage in a disinterested and dispassionate assessment. CremaDES reports that “the proponents of third party financing in international arbitration see the presence of the professional financier as a guarantee that there is solid basis for the claim” and that “the respondent should reconsider his defense with regard to a claim that has passed the study of a financing entity and its advisors.”

81. Proponents thus believe that TPF will not lead to the financing of frivolous or unmeritorious claims because funders will only fund a claim which has a reasonable chance of succeeding, since its investment will otherwise be for naught. The simple fact that TPF agreements are customarily


entered into after the party decided to pursue the claim further rebuts the argument that TPF will lead to weak and unmeritorious claims. The Texas Court of Appeals followed this reasoning in the *Anglo-Dutch Petroleum v. Haskell* case with respect to the opinion that TPF will not lead to funding frivolous claims:

“Presumably, prior to making an investment pursuant to a similarly structured agreement, an investor would consider the merits of the suit and make a calculated risk assessment on the probability of a return on its investment. An investor would be unlikely to invest funds in a frivolous lawsuit, when its only chance of recovery is contingent upon the success of the lawsuit.”

82. Conversely, detractors voice a deep concern that TPF will in fact prompt frivolous claims and increase the volume of cases because TPF makes it possible for claims of questionable merit to be litigated or put through arbitration. As opposed to contingency fee arrangements, funders supposedly do not have the same incentives as lawyers working on a contingency fee basis. Detractors

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153 Empirical evidence of this can be found in Australia, where an estimated 16.5% increase in litigation was reported after liberalising its attitude towards TPF. See U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, *Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States*, October 2009, 9 and http://legaltimes.typepad.com/files/thirdpartylitigationfinancing.pdf.

claim that funders lack the ethical duty to advise clients when claims are frivolous and that lawyers – when they are working on contingency basis – rather spend their time on cases that are likely to be successful, as opposed to cases with a low probability of success. Moreover, they also assert that the likelihood of a lawsuit’s success is only one component. Another component is the potential amount of recovery. It could therefore be possible that the potential recovery outweighed the likelihood of actually achieving that recovery. KANTOR explicitly states that:

“These companies – like all sophisticated investors – will base their funding decisions on the present value of their expected return, of which the likelihood of a lawsuit’s success is only one component. The other component is the potential amount of recovery. If that potential recovery is sufficiently large, the lawsuit will be an attractive investment, even if the likelihood of actually achieving that recovery is small.”

83. Furthermore, some commentators fear that funders will have no qualms about creating portfolios consisting of high-risk claims (i.e. frivolous or unmeritorious claims) and low-risk claims (i.e. claims with a good chance of success) to hedge the high-risk claims and sell them to third-party speculators as derivatives. Third-party speculators would thus have the possibility to invest in and profit from frivolous claims that would otherwise, when sold individually, not have a market with speculators. Furthermore, funders would supposedly have less incentive to perform a meticulous due diligence to decide whether the claim is frivolous because the risk of loss would be spread among

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numerous investors. In this respect, BEISNER even impudently declared that “[t]he whole theory is to take the legal system and turn it into a stock market.” TPF could thus, in time, evolve into intricate financial engineering involving other related financial products, such as credit default swaps. However, it remains to be seen how the market will develop and whether demand will continue to grow in the years ahead. The author nevertheless deemed it necessary to identify this issue due to the potential impact it could have on further development of TPF. It can be argued that the non-negligible risk of an increase in frivolous disputes due to TPF is heightened when portfolios of high-risk claims are created and sold as derivatives. This is in contrast to the funding on a ‘case-by-case’ basis, because in the latter situation there is ordinarily only little incentive for funders to finance frivolous claims, whereas in the former situation funders could hedge the downside risk by including some low-risk claims as well. Accordingly, funders will have a higher risk appetite when funding a portfolio of cases and are more likely to finance frivolous claims.

84. To date, there is however no conclusive evidence that TPF of claims promotes frivolous claims. Nevertheless, it is alarming if funders such as SMITH state that “the perception that you need strong merits is wrong – there’s a price for everything.” It thus remains to be seen – while awaiting the arrival of hard data on the effect of TPF in international commercial arbitration – whose side is right regarding the relationship between TPF and frivolous claims.

6. Third-party funding in international investment arbitration

85. DE BRABANDERE and LEPETETAK consider the surge in arbitral proceedings and the publication of the majority of arbitral awards in international investment law as another important

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reason for the increase of TPF in international investment arbitration.\textsuperscript{164} As a result, funders will obtain better knowledge of the possible outcome of the proceedings and can decide more objectively whether the investment can be justified from a business point of view. As noted above,\textsuperscript{165} due to the lack of consistently publishing arbitral awards in international commercial arbitration, this argument only applies for international investment arbitration and not for international commercial arbitration.

86. Furthermore, investment arbitration is arguably more attractive than commercial arbitration at this moment for TPF for the following reasons. First and foremost, investments in international investments claims tend to be more lucrative because investment arbitration claims usually exceed the amount of compensation requested in international commercial arbitration.\textsuperscript{166} Second, the ICSID Convention is more appealing to funders than the New York Convention because awards can easily be recognized and enforced through the former. The New York Convention, even though this convention facilitates enforcement, nevertheless contains possibilities for review by domestic courts. On the other hand, article 54(1) of the ICSID Convention states that there are no review possibilities by national courts.


\textsuperscript{165} Supra 2, no. 5.

\textsuperscript{166} However, some funders, such as Calunius Capital, state that only very few funders want to get involved in investment treaty arbitrations because of the longer investment period due to longer case duration and more pronounced risk profiles. CALUNIUS CAPITAL LLP, Memorandum: A European Perspective, 15th June 2011, 2 and \url{www.calunius.com/media/1549/tpf%20of%20international%20arbitration%20claims%20the%20newest%20new%20new%20thing.pdf}; conversely, there are also funders and commentators who regard TPF of investment arbitration cases more appealing than commercial arbitration because of the potential for even larger recoveries. See e.g. C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, \textit{Ethics in International Arbitration}, Oxford University Press, forthcoming June 2014; S. SEIDEL, “Third Party Capital Funding Of International Arbitration Claims: An Awakening And A Future”, \textit{Financier Worldwide} July 2012, 37 and \url{www.financierworldwide.com/login.php?url=article.php%3Fid%3D9500}; A. MEYA, “Third-party funding in international investment arbitration” in B. CREMADES and A. DIMOLITSA (eds.), \textit{Dossier X: Third-party Funding in International Arbitration}, Paris, ICC Publishing S.A., 2013, 124.
CHAPTER V. DUE DILIGENCE

1. Funders

87. A funder’s decision to fund a claim or defence is typically an investment decision, which requires a rigorous investigation because the investment can result both in a substantial benefit and in a sizeable loss. When contemplating whether the claim is unmeritorious or, on the contrary, serious enough to merit funding, it behoves funders to undertake an expensive and extensive vetting process, taking into account various factors that could influence the financial risks it is being asked to shoulder.167 Financing a claim thus requires knowledge on international arbitration as such, and at the same time a thorough knowledge of international finance. However, little is known about the methodology of funders in taking the decision to finance a certain arbitral procedure.

88. Funders may become involved in a claim at the very outset of the proceedings, even before a claim is filed or before the claimant has hired legal counsel. Alternatively, the arbitral proceedings may have already begun when funders become involved.168 Unsurprisingly, there is less need for extensive due diligence if the arbitral proceedings are already in a developed stage.

89. Various factors should be considered before entering into a funding agreement.169 These factors include: (i) the prospects of success of the claim;170 (ii) possible counterclaims; (iii) the terms of the arbitration agreement; (iv) the arbitral institution and composition of the tribunal; (v) the seat of the arbitration; (vi) the substantive law of the dispute; (vii) the value of the claim in comparison to the

167 Only a small percentage of the claims that seeks funding eventually end up with funding. For instance, in Fulbrook Management, approximately one claim out of twelve requests end up being funded. S. SEIDEL, “Investing in commercial claims, nutshell primer”, Fulbrook Management Publications 2011, 15 and http://fulbrookmanagement.com/publications/Nutshell-Primer.pdf; Harbour Litigation Funding and Calunius Capital reportedly agree to fund around 8% of the reviewed requests. C. VELJANOVSKI, “Third-Party Litigation Funding in Europe”, 8 J.L. Econ. & Pol’y 2012, 420.
likely costs and risks of pursuing the claim;\textsuperscript{171} (viii) the creditworthiness of the client and the opposing party and the prospects of recovery;\textsuperscript{172} (ix) the duration and merits of the proceedings; and (x) the possibility of the lawyers sharing risks through the success fee.\textsuperscript{173}

2. Clients

90. By the same token as the funders, the client has to perform an assiduous due diligence process with respect to the funder. Before entering into a funding agreement, the claimants and their lawyers should do careful due diligence on the different funders, both in relation to the funder’s financial standing and track record and the experience and competence of its staff.\textsuperscript{174}


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SECOND PART – ISSUES REGARDING THIRD-PARTY FUNDING
CHAPTER I. LEGAL ETHICS AND DOCTRINES AND THIRD-PARTY FUNDING

91. There are still some legal doctrines and ethical rules in existence that could obviate the TPF industry from developing in some jurisdictions because the doctrines and rules in question can affect, or at least call into question, the validity and enforceability of TPF agreements. Considering the competition playing between countries and arbitral institutions to attract arbitral proceedings, it is vital to know if TPF agreements will be recognised and enforced in subsequent court proceedings. If this is not the case, parties may be reluctant to go to the jurisdiction in question.

92. The doctrines of maintenance and champerty have had some influence on the overwhelming development of TPF in common law countries. Maintenance and champerty are separate doctrines, but are so closely related that they are often addressed together in scholarly work. The interpretation and application of these doctrines differ significantly in the different common law jurisdictions.

93. The debate on ethical issues in civil law countries is more focused on professional attorney ethics rules, rather than on the application of the doctrines of maintenance and champerty to TPF relationships. Prima facie, these jurisdictions appear to be free from the antiquated doctrines of maintenance and champerty and their possible constraints of TPF arrangements.

94. The following paragraphs will examine the definition and the historical developments of the doctrines of maintenance and champerty. Additionally, this section will look at the doctrine of usury and some other ethical issues surrounding TPF that could prohibit or limit attorney collaboration with funders. Each subsection will conclude by considering how the national laws and local rules may affect TPF of international arbitration claims.

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1. National law limitations on funding agreements

1.1. Maintenance and champerty

1.1.1. Definition

95. As it will become clear from the definitions hereafter, TPF can be considered a type of financing, for which the ancient doctrines of maintenance and champerty were originally created. Maintenance is the “assistance in prosecuting or defending a lawsuit given to a litigant by someone who has no bona fide interest in the cause; meddling in someone else’s litigation.” Champerty is “an agreement between an officious intermeddler in a lawsuit and a litigant by which the intermeddler helps pursue the litigant’s claim as consideration for receiving part of any judgment proceeds.”

96. These doctrines are sometimes coupled with barratry, which is the “vexatious incitement to litigation, especially by someone soliciting potential legal clients.” Put simply in the words of the USSC, "maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.”

97. By definition, these doctrines prohibit TPF. However in practice, as will be indicated hereafter, the restrictions imposed by these doctrines are often being relaxed or have been abandoned.

1.1.2. History

98. Traditionally, the participation and investment of third parties in domestic litigation has been frowned upon because the proceedings might become corrupted by allowing parties, who are unconnected with the merits of the dispute and whose main motive is making a profit, to participate in the procedure.

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179 Barratry is a separate doctrine, but is often consumed by the doctrines of maintenance and champerty in both literature and case law; hence, the focus on maintenance and champerty in this section.

99. Maintenance and champerty were originally introduced to prevent rich and powerful men from abusing the courts by financing disputes, merely for the purpose of distressing enemies, despite having no legitimate interest in the dispute. Since the courts were too weak at the time to control such abuses, a blanket prohibition was imposed to ban the problem.\textsuperscript{181} Thus the situation in the nineteenth century in the U.K. – where the doctrines were born – was that maintenance and champerty were considered unethical and against public policy and therefore made illegal.\textsuperscript{182} Today, champerty prohibitions are aimed at discouraging frivolous litigation,\textsuperscript{183} diminishing resistance to settlement,\textsuperscript{184} and reducing interference with the attorney-client relationship.\textsuperscript{185}

100. In theory, some common law jurisdictions continue to characterize the intervention of a third party as dishonest.\textsuperscript{186} In practice, however, there has been a substantial relaxation of these rigid ethical


\textsuperscript{183} For instance in Hong Kong, maintenance and champerty continue to be regarded as criminal offences under local law. See E. BROOMHALL, “Hong Kong reviews laws for third party funding in arbitration”, \textit{Legal Week} 31 October 2013, \texttt{www.legalweek.com/legal-week/news/230406/hong-kong-mulls-new-laws-for-third-party-funding-in-arbitration}.
regulations in many jurisdictions and outright repealed in others.\textsuperscript{187} Nowadays, the traditional statutory and case law prohibitions and criminal and tortious consequences of champerty and maintenance have mostly faded away and have been abolished, which has resulted in several jurisdictions becoming more supportive and flexible towards TPF.\textsuperscript{188} The result has been the healthy and laudable development of a solid, sophisticated and growing market and industry with an increasing number of parties using, or contemplating using TPF.

101. Lord NEUBERGER, the President of the U.K. Supreme Court, enumerates the current situation and conception of the doctrines in the U.K. by expressing the following:

“[T]he public policy rationale regarding maintenance and champerty has turned full circle. Originally their prohibition was justifiable as a means to help secure the development of an inclusive, pluralist society governed by the rule of law. Now, it might be said, the exact reverse of the prohibition is justified for the same reason.”\textsuperscript{189}

102. Nevertheless, maintenance and champerty are not dead just yet. Courts can still invalidate a TPF agreement on the grounds that the contract is champertous and thus contrary to public policy.\textsuperscript{190} Furthermore, some commentators and organisations, such as the Institute for Legal Reform of the U.S.


\textsuperscript{189} D. NEUBERGER, \textit{From Barratry, Maintenance and Champerty to Litigation Funding}, Harbour Litigation Funding First Annual Lecture 8 May 2013, 20-21 and http://adam1cor.files.wordpress.com/2013/05/lord-neuberger-harbour-litigation-lecture-8-may-2013.pdf.

Chapter I. Legal Ethics and Doctrines and Third-Party Funding

Chamber of Commerce (“ILF”), recommend a renewal of the former prohibition of the Anglo-Saxon champerty law.  

103. The rules regarding TPF in litigation vary from state to state in the U.S. and so does the attitude towards maintenance and champerty. It appears that the doctrines have fallen by the wayside since the mid-nineteenth century. Some states retain the common law doctrines, where others have renounced them. The highest courts of several states have explicitly rejected champerty and maintenance doctrines. For instance, the 19978 Massachusetts Supreme Court decision in Saladini v. Righellis is typical in this regard. In ruling that the doctrines of maintenance and champerty shall no longer be recognised in Massachusetts, the court reasoned that “the champerty doctrine is [no longer] needed to protect against the evils once feared: speculation in lawsuits, the bringing of frivolous lawsuits, or financial overreaching by a party of superior bargaining position.”

104. Conversely, the Ohio Supreme Court ruled in Rancman v. Interim Settlement Funding Corporation in 2003 that a funding company’s advance to a litigant in return for a percentage of the recovery was void under principles of champerty and maintenance.

105. Lying in the middle of these extremes are state courts that have limited – but not abolished – the effect of these ancient doctrines. For instance in the 1996 Kraft v. Mason case, a Florida appellate court held that an arrangement in which the litigant obtained TPF in exchange for a certain percentage

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195 Rancman v. Interim Settlement Funding Corp., 99 Ohio St.3d 121, 2003-Ohio-2721.
of the ultimate recovery was not prohibited as such by champerty because the funder had neither incited the litigation nor set the terms of the funding agreement.\textsuperscript{196}

106. Finally, one could regard these doctrines as an already existing legal framework for TPF, hence making further regulation\textsuperscript{197} redundant. However, these doctrines predate the TPF industry and are therefore less than ideal frameworks, especially considering the inconsistency of its form and application among different jurisdictions, as well as its lack of relevance to modern business transactions.\textsuperscript{198}

1.2. Usury

107. Usury laws prohibit loans at abuse interest rates\textsuperscript{199} and are akin to the champerty doctrine with respect to their historical significance.\textsuperscript{200} The obvious question that emerges here is whether TPF agreements can be qualified as loans with respect to the applicability of usury because it \textit{prima facie} appears that usury regulations would render most funding agreements illegal.

108. For instance in Germany, the courts frame TPF agreements by referring to the concept of usury. The limitation imposed by usury, eventually caused funders to curtail their interests in the award.\textsuperscript{201} Usury is a convenient concept to avoid abuses by the funders. However, it remains manifestly uncertain whether all TPF agreements can be qualified as loans.\textsuperscript{202} As for the U.S., the law in most states consider TPF agreements to be investments rather than loans due to their contingent nature.\textsuperscript{203} The latter implies that funders are therefore not subject to the statutory limits on interest rates imposed by usury laws.


\textsuperscript{197} \textit{Infra} 94-97, nos. 259-267.


\textsuperscript{199} For an overview of the usury rate caps in recently filed legislation on lawsuit loans in the U.S., see V. SHANNON, “Recent Developments in Third-Party Funding”, 30(4) \textit{J. Int. Arb.} 2013, 449-450.


\textsuperscript{202} \textit{Supra} 13, no. 38.

109. Nevertheless, local prohibitions against usury can, under certain conditions, still affect the validity of funding agreements if the funder seeks a high rate of return if the claim is successful because usurious agreements are against public policy and can be declared void for that reason.\textsuperscript{204}

1.3. National limitations in international arbitration

110. The various doctrines were originally aimed at preventing certain practices in the context of litigation. That leaves open the question whether these doctrines apply in the private world of arbitration. There is a possibility that the remaining restrictions or prohibitions imposed by these doctrines do not have any bearing on arbitral disputes due to the inapplicability of the public policy protection of the national civil justice system, which is the basis for the prohibitions in the court litigation context, in the private world of arbitration where the will of the parties is generally paramount.\textsuperscript{205}

111. There are a number of possibilities whereby the doctrines could play in international arbitration. First, the parties and the arbitral tribunal have to comply with the mandatory \textit{lex loci arbitri}. Second, a court can, in set-aside or enforcement proceedings, impose its view on the validity of TPF agreements or decide that the TPF agreement is contrary to public policy. One can also think of the situation where a funded claimant secured a favourable settlement or award and is subsequently not so keen anymore on sharing the agreed amount with the funder. The funded client could subsequently attempt to obtain an order from a local court to invalidate the funding agreement, which would free the funded party from its obligations.\textsuperscript{206}

112. However, there are several reasons to believe that champerty and related doctrines do not operate with the same force for funding agreements in international arbitration.\textsuperscript{207} In other words, there is a legitimate doubt that these doctrines could or would be applied to annul arbitral awards for the following reasons. As noted above,\textsuperscript{208} the rationale behind the doctrines was protecting public courts from vexatious litigation. It is debatable whether this rationale should be extended to funding of


\textsuperscript{205} See generally S. SEIDEL, “Third-party investing in international arbitration claims: To invest or not to invest? A daunting question” in B. CREMADES and A. DIMOLITSA (eds.), \textit{Dossier X: Third-party Funding in International Arbitration}, Paris, ICC Publishing S.A., 2013, 22; see e.g. Fausone v. US Claims, Inc., 915 So. 2d 626 (Fla. Dist. Ct. App. 2005), where the Court upheld the confirmation of the arbitral award in which it was determined that the funder could recover unpaid amounts under the funding agreement.


\textsuperscript{208} Supra 41, no. 99.
claims in arbitration. As for the U.K., the issue was settled in 1998 in the above-mentioned case of Bevan Ashford v. Geoff Yeandle, in which it was decided that champerty does extend to arbitration. However, WILLEMS notes that “the common law has never had any difficulty with accepting that these principles do not apply to litigation or arbitration abroad, as English public policy is not applied extraterritorially.”

113. The Otech Pakistan v. Clough Engineering case from the Singapore Court of Appeal is illustrative in this regard. The court expressly stated that “it would be artificial to differentiate between litigation and arbitration proceedings and say that champerty applies to the one because it is conducted in a public forum and not the other because it is conducted in private.”

114. Even if the prohibitions imposed by champerty and related doctrines would apply to funding agreements that are subject to arbitration, it is still a matter of debate and uncertainty whether these prohibitions would have some, if any, effect on the arbitral proceedings as such or on resulting awards. As noted above, disregarding mandatory lex loci arbitri can indeed be a ground for annulling an award on the basis that “the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place.” However, generally only mandatory procedural law can be a ground for annulling an award, and not mandatory substantive law, which champerty and related doctrines are generally regarded to be. The doctrines are generally invoked to obtain criminal sanctions or tortious liability and not to refuse the relief of the funder in the case, nor to affect any other procedural aspect.

115. Mandatory substantive law can only be a ground for the annulment of an award if that law is of public policy. However, the author shares the view of ROGERS that champerty and related doctrines are not of public policy, since they are aimed at the parties to the funding agreement and not at the outcome of the funded dispute. Nevertheless, several commentators still assume that awards could be refused enforcement for reasons of public policy, despite the fact that there are no publicly

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210 Contra Giles v. Thompson [1993] UKHL 2, [1994] 1 AC 142, [1993] 3 All ER 321 were the Court acknowledged that champerty did not apply in arbitral proceedings.
212 Otech Pakistan Pvt. Ltd. v. Clough Eng’g Ltd., [2006] SGCA 46.
213 Supra 45, no. 111.
214 Art. V(d) of the New York Convention.
215 Supra 41-42, no. 100.
216 Oil, Inc. v. Martin, 381 Ill. 11, 44 N.E.2d 596 (1942).
available cases where recognition and enforcement has been refused simply because a funder was involved in the proceedings.\textsuperscript{218}

116. Moreover, it is also unlikely that funding agreements are within the reach of the \textit{lex loci arbitri} – and by extension enforcement jurisdictions – because these agreements are not part of arbitration agreements. Invalidating funding agreements which have no formal relationship to the seat of arbitration would imply the extraterritorial application of national law. \textsc{Rogers} states that this is only possible “if one of the parties to the funding agreement (the funder, the party, or the attorney) were a local citizen, or the agreement bore some other relationship to the seat, would extraterritorial application of laws against champerty be a reasonable extension.”\textsuperscript{219}

117. In the quintessential setting of TPF in international commercial arbitration, the parties to the funding agreement are not locals and the funding agreement would stipulate another substantive law by which it would be governed than the substantive law of the seat.\textsuperscript{220} Extraterritorial application of champerty or related doctrines to invalidate funding agreements would arguably, in most cases, be a proverbial ‘bridge too far’.

\textbf{1.4. Conclusion}

118. The lesson to be drawn from this discussion is that TPF in international arbitration is a far too recent phenomenon without clear national precedents or established practices to discover trends as to the application of these doctrines in this industry. There have been jurisdictions that consider TPF agreements to be within the purview of the courts when deciding on enforcing, annulling or setting aside arbitral awards.\textsuperscript{221} The author expects that this issue will continue to be subject to lively and acrimonious debate, until the TPF industry accrues big enough so that key jurisdictions will have to determine the effects of the doctrines on TPF agreements.

\textbf{2. The attorney’s ethical duties}

119. It should be noted that the following paragraphs are more of a theoretical nature due to the fact that local ethical rules are not generally deemed to apply to counsel for parties in international

\textsuperscript{220} Ibid.
arbitrations. Nevertheless, it seems that some funders are reluctant to accept that none of the ethical rules will apply and are therefore still cautious, for instance when transferring legal documents from and to the client’s attorney.

120. It is not within the ambit of this discussion to identify and analyse the various domestic procedural law provisions regarding the attorney’s ethical duties. Some provisions will nevertheless be mentioned to serve as an illustration for the reader.

2.1. Privilege

121. In order to perform a proper due diligence and to decide whether or not to fund, funders need access to all the pertinent information to the claim, which can be in the possession of both the claimant and the claimant’s lawyer. However, the risk exists that the respective documents or information become discoverable in certain jurisdictions. This is a question relating to privilege or professional secrecy issues that may vary depending on the jurisdictions involved. It should be noted that the U.S. is one of the most challenging jurisdictions in this respect. It is therefore crucial for funders to discover whether the respective jurisdiction offers protection against disclosure orders.

122. Documents prepared by a lawyer or documents for the purpose of the dispute generally enjoy a legal privilege: either the attorney-client or work-product privilege. There is a risk that this legal privilege will be waived when these documents are given to the funder, or that communications between the funder and the funded claimant and/or claimant’s lawyer about the claim will not be protected by privilege in jurisdictions which do not recognize a common-interest privilege.

123. The common-interest privilege is considered an exception to the attorney-client privilege.\(^{225}\) It protects communications when two or more clients simultaneously consult with an attorney on matters of common interest. The idea behind this privilege is to give persons, who share a common interest, the ability to communicate with each other and with their attorneys in order to prosecute or defend their claims more efficaciously.\(^{226}\) That leaves open the questions whether funders are included in the group of persons to whom the common interest privilege applies and whether the attorney-client privilege and common interest privilege applies to confidential information in international arbitration. To date, there are absolutely no definite answers available.\(^{227}\) AFFAKI states that questions like these are most likely to be resolved on a ‘case-by-case’ basis.\(^{228}\)

124. However, as practice has indicated, the risk of a waiver of privilege has to be put into perspective because the author is, to the best of his knowledge, not aware of a single case or decision that would have led to the loss of privilege of communication with a funder in Europe. Nevertheless, the lawyer should fully explain to the client the risks associated with the disclosure.

125. As for the U.S., two illustrative cases can be found where the question of the applicability of the common interest privilege regarding funders arose. The first reported case is the Leader Techs. v. Facebook case in which the court found that the common interest privilege did not exist in this case because the potential funders, who received documents from the plaintiff, merely had a commercial interest in the case and the common interest privilege does not attach to such interests.\(^{229}\) In contrast, in the case of Devon IT, Inc. v. IBM Corp., the court ruled that the documents shared between the plaintiff and its funder were protected by the common interest privilege.\(^{230}\) The author acknowledges

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229. Devon IT, Inc. v. IBM Corp., No. 10-2899, 2012 WL 4748160; for a more elaborate discussion on these two cases, see C. LAMM and E. HELLBECK, “Third-party funding in investor-state arbitration” in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 111; NEW YORK STATE BAR ASSOCIATION, Report on the Ethical Implications of Third-Party Litigation Funding, 16 April 2013, 7-9 and
that these two cases involved U.S. federal litigation and *prima facie* may seem irrelevant for international arbitration. Nonetheless, comparable considerations could apply in international arbitrations, depending on the applicable law governing the proceedings. While awaiting further developments, the author concludes that the issue of the applicability of common interest privilege regarding funders remains unsettled.

126. In practice, to elude discussions on whether the privileges apply and to protect themselves against disclosure requests, the funder and the funded party customarily enter into a non-disclosure agreement at the very outset or they agree on a confidentiality clause in the funding agreement.231 The author foresees that this will remain the common practice until the issue is settled.

2.2. The beneficiary of the attorney’s ethical duties

127. As a general principle, the attorney’s ethical duties are first and foremost those that he or she has towards his or her client. In the context of TPF, the question arises whether the funder can be considered the attorney’s ‘client’. It can be argued that the funding company becomes a client when financing one of the parties in the arbitration. However, some of the attorney’s duties cannot be shared, which makes this issue even more significant. For instance, under French law,232 the attorney-client privilege233 cannot be divided and the attorney cannot be released from it by its client.234 This implies that in those jurisdictions, the funder does not enjoy the same attorney-client privilege as the funded client.

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232 Règlement Intérieur National, art. 2.1; Cass. 1ère civ., 6 April 2005, n° 00-19.245.
233 Supra 48-50, nos. 121-126.
128. It is conceivable nevertheless in current TPF practice that the original client (i.e. the funded party) could withdraw from the case. In that case, the funder would be the only party giving instructions to the attorney and would be the one paying his or her fees. This could arguably justify a requalification as the ‘client’. Moreover, it can be argued that in the event the funder is allowed to give instructions to the attorney, certain duties of the attorney, such as the duty to advise and the duty of loyalty, could be extended to the funder. As it will be discussed in more depth further on, qualifying the attorney as a client or extending certain duties of the attorney to the funder could give rise to conflicts of interest.

2.3. The lawyer’s ‘duty-to-know’ and ‘duty-to-tell’ about third-party funding

129. Considering the growth of TPF, another question that arises is whether lawyers have a so-called ‘duty-to-know’ and ‘duty-to-tell’ their clients about TPF. This robust duty can be divided into two: (i) an ethical duty; and (ii) a legal one. First, the duty to advise is, inter alia, one of the attorney’s main ethical obligations. This duty may be found in several explicit and implicit rules in various jurisdictions. For example, in the U.K. the solicitor has to, under the SRA Code of Conduct 2011 (“SRA Code”), “discuss with the client how the client will pay.” This obligation could include the duty to tell the client of the possibility of obtaining TPF as such, as well as the possible consequences of the funding agreement, in particular regarding the potential conflicts of interests that could arise.

130. The question remains whether the attorney has this duty when he is not aware of the presence of a funder. The vast majority of the participants at the Roundtable Discussions seemed to believe that an additional obligation cannot be placed on the attorney if he or she is unaware of the funding. This author concurs with the majority, especially considering that the funding agreement often contains a

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236 Infra 55-57, nos. 143-146.

237 Infra 57-61, nos. 147-153.


239 SRA Code, r.2.03(1)(d), see www.sra.org.uk/Solicitors/code-of-conduct/rule2.page.


confidentiality clause,\textsuperscript{242} which prohibits the funded client from disclosing the existence of the agreement.

131. As for the legal duty, SEIDEL notes that this can be taken from various legal sources. For instance in the \textit{Adris v. Royal Bank} decision of 2010, the Queen’s Bench found that a solicitor’s failure to obtain costs insurance\textsuperscript{243} for his client, protecting against adverse costs that later were incurred, was a “gross breach of the Consumer Credit Act of 1974 s. 78.”\textsuperscript{244} The lawyer has to provide his or her client with competent advice, \textit{in casu} about the possibility of acquiring insurance.\textsuperscript{245}

\textsuperscript{242} \textit{Supra} 50, no. 126.
\textsuperscript{243} \textit{Supra} 11-13, nos. 33-37.
\textsuperscript{244} \textit{Adris & Ors v. The Royal Bank of Scotland Plc} [2010] EWHC 941 (QB).
CHAPTER II. FULL DISCLOSURE OF THIRD-PARTY FUNDING AGREEMENTS?

132. Compulsory disclosure of the presence of a funder has become a fiercely debated issue with widespread importance and relevance. It will be shown in this chapter that, to date, no mandatory disclosure obligation as such exists. The issue of finding an ideal balance between the need for disclosure and the need for confidentiality is now being addressed by commentators, practitioners and funding companies. Such transparency rules could undermine the strength of international commercial arbitration because arbitration as a method for dispute resolution derives so much of its value from its strict confidentiality.\textsuperscript{246}

133. This issue is of paramount importance due to the numerous interests involved in international arbitration and the legal questions that relate to it. Questions such as: should there be a disclosure obligation? What should be disclosed and to whom? When should a funding agreement, or its existence, be disclosed? What is the rationale for requiring such a disclosure? Can tribunals use their discretion to intervene in or take into consideration the relationship between the funder and the funded party, in particular in view of the allocation of costs?

134. This chapter aims at addressing some of these questions by discussing both the reasons that could justify a potential obligation to disclose funding agreements and the possible scope of such an obligation. Finally, this section will conclude by discussing a proposal for a disclosure obligation of TPF agreements.

1. Is there a disclosure obligation for third-party funding?

135. Many national courts have already settled and defined the issue of which financial interests are to be disclosed. For example, the USSC determined that a party’s parent corporations and any public shareholder owning more than 10\% of the party’s stock should be identified and thus needs to be disclosed.\textsuperscript{247}

136. Conversely, funders - whether institutional funders, banks or insurers\textsuperscript{248} – are, to date, not subject to a disclosure obligation in international arbitration.\textsuperscript{249} The involvement of a funder in an

\textsuperscript{246} See generally S. SEIDEL and S. SHERMAN, “‘Corporate governance’ rules are coming to third party financing of international arbitration (and in general)” in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 40.

\textsuperscript{247} See Rule 29(6) of the Rules of the USSC.

\textsuperscript{248} Supra 17, 50-51.

international arbitration case will thus most often be unknown or unknowable because there is no specific disclosure obligation as such in any of the rules of the leading arbitral institutions.

137. However, there are situations where the arbitral tribunal or the opposing party will obtain knowledge of the involvement of a funder; for instance when the funding relationship is disclosed voluntarily\footnote{Voluntary disclosure is permissible in international investment arbitration due to the largely transparent nature. See for instance Oxus Gold PLC v. Republic of Uzbekistan et al., UNCITRAL, 31 August 2011 in which the claimant (Oxus Gold) voluntarily stated in a press release that it obtained TPF to fund their dispute with Uzbekistan. The press release is available at: www.reuters.com/article/2012/03/01/idUS101378+01-Mar-2012+RNS20120301; see also for a discussion of this case, A. MEYA, “Third-party funding in international investment arbitration” in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 131-132.} or when the funder of funded party is under an obligation to disclose such information because it is a listed company.\footnote{For instance Burford Capital is listed on the London Stock Exchange. See www.londonstockexchange.com/exchange/prices-and-markets/stocks/summary/company-summary.html?fourWayKey=GG00B4L84979GGGBXASQ1.} Nevertheless, as a general principle, funders and funded parties are not subject to a disclosure obligation.

2. Rationale behind a disclosure obligation of third-party funding agreements

138. The key question in the context of international commercial arbitration is whether – and, if so, to what extent – the funding relationship as such and perhaps even the contents of the funding agreements should be disclosed. The ascertainment of the existence of a funding arrangement is desirable for three reasons in particular. First, disclosure is arguably necessary to avoid possible conflicts of interest and to ensure that the arbitrator’s impartiality and independence are maintained. Second, disclosure is also arguably necessary to assess whether the funded party should be subject to an order for security for costs and to assess the potential influence on the allocation of costs. Lastly, disclosure is arguably recommended in order to give arbitral tribunals the opportunity to consider the need to impose a duty of confidentiality on funders. The former reason will be discussed first.

2.1. Preventing conflicts of interest

139. Due to the growing TPF industry, potential conflicts of interest are arising in international arbitration. With regard to conflict of interest, the distinction has to be made between: (i) conflicts of...
interest in the three-cornered relationship between the funded party, the funded party’s lawyer, and the funder; and (ii) conflicts of interest with respect to the appointed arbitrator(s).

2.1.1. Three-cornered relationship between funded party – funded party’s lawyer – funder

140. Although a typical funding agreement is entered into between a client and a funder, it cannot be qualified simply as a plain bilateral relationship due to the presence of the client’s lawyer. As this section will describe, this ‘three-cornered relationship’ can give rise to numerous potential conflicts of interest.

141. The problems that can arise – both at the stage of concluding the funding agreement and the stage of the arbitration proceedings as such – are usually the result of a conflict between: (i) the client’s interest (i.e. achieving the most favourable outcome); (ii) the attorneys interest (i.e. receiving payment for hourly fees); and (iii) the funder’s interest (i.e. achieve the biggest return on investment).

142. After discussing the issue of funders controlling the proceedings and the correlated conflicts of interest, this section will examine the question of how to avoid these kinds of conflicts.

A. Control over the proceedings

143. The main predicament with TPF is the addition of a different interest in the proceedings (i.e. the interest of the funder), which is to make the largest possible return on its investment. Since funders do not have an interest in the substantive issues of the proceedings and their sole goal is (usually) making a profit, the inherent risk exists that parties might bequeath the control of the arbitral proceedings to the funder. Funders want to protect their investments by being involved in the management of the case and thus exercising some control over the proceedings. However, the level

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254 There are exceptions, such as situations where the funding can be qualified as pure donations or free financial assistance. Supra 15, no. 44.

of control differs from funder to funder, ranging from simply receiving progress reports, to being the *de facto* party that appoints the attorneys and the arbitrator and who conducts settlement talks. Thus, some funders do not get involved in the management of cases and see themselves as mere passive investors in the client’s case, whereas others shall exercise strategic control over the proceedings to monitor their investment.

144. The claimant’s lawyer will likely be asked to provide regular reports to enable the funder to monitor progress of the claim and to ensure compliance with the claimant’s obligations under the funding agreement. The funders present at the Roundtable Discussions had a consensus regarding the monitoring of the legal team. They were all of the opinion that they should not directly instruct them, but only monitor them on a monthly basis. This can be done for instance by including monthly monitoring clauses in the funding agreement.

145. TPF entities can thus be divided into two groups with regard to the exercised amount of control: (i) the ones that have a ‘hands-off’ approach; and (ii) the ones that have a ‘hands-on’ approach. A ‘hands-off’ approach is what most funders wield and it implies that the funder takes...

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Some commentators use the terminology of ‘passive’ and ‘active’ funding to make the distinction regarding the exerted control by the funders. See e.g. C. VELJANOVI{\v s}KI, “Third-Party Litigation Funding in Europe”, 8 *J.L. Econ. & Pol’y* 2012, 408 et seq.

VELJANOVI{\v s}KI interviewed several funders that are based in the U.K. – and thus often restricted by the prohibitions imposed by the doctrines of maintenance and champerty *(supra* 40-47, nos. 95-118) – and they all

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http://old.nysba.org/AM/Template.cfm?Section=Commercial_and_Federal_Litigation_Section_Reports&template=CM/ContentDisplay.cfm&ContentID=200115

http://old.nysba.org/AM/Template.cfm?Section=Commercial_and_Federal_Litigation_Section_Reports&template=CM/ContentDisplay.cfm&ContentID=200115
CHAPTER II. FULL DISCLOSURE OF THIRD-PARTY FUNDING AGREEMENTS?

no control over the claim. A ‘hands-on’ approach means that the financing entity offers support for the case and not that it has control over it, as the decisions remain to be taken by the client and its counsel. ROSS asserts that “[t]here is a ‘push’ by funders to get more control of cases and sell more services.” It remains to be seen whether the most commonly applied ‘hands off’ approach will be replaced in the future by the ‘hands on’ approach.

146. The influence of the funder on the claim management depends on the contractual arrangements between the funder and claimant and on the application of the rules regarding maintenance and champerty to the particular funding agreement. As explained above, the doctrines of maintenance and champerty, as they apply to arbitration, are not settled and will likely be clarified piecemeal as disputes arise and come before arbitral tribunals and domestic courts. Prima facie, the issue of contractually transferring control does not seem that pressing in international commercial arbitration, considering the private and contractual nature of arbitration and because “the funding agreement between the client and the third-party funder is an arm’s-length transaction and does not involve a fiduciary relationship – in contrast to the lawyer-client relationship – the client may legitimately bestow rights on the third-party funder, including the right to discharge counsel and make strategic decisions about the course of the litigation.”

B. Potential conflicts of interest

147. The lawyer acting for the claimant remains at all times the claimant’s lawyer and owes duties and responsibilities solely to the claimant. However, TPF can pose a threat for the foundation of the attorney-client relationship because of the control some funders exert over the proceedings and the lawyer. Several commentators warn that too much control over the proceedings by the funder could indeed be a threat for the attorney-client relationship. See e.g. M. STEINITZ, “Whose Claim Is This Anyway? Third-Party Litigation Funding”, 95 Minn. L. Rev. 2011, 1324-1325; D. RICHMOND, “Other People’s Money: the Ethics of the
are given by someone else” is “indicative behaviour” of actions that are contrary to the attorney’s obligation to act in his or her client’s interest.²⁶⁸ The following is a good example of a possible conflict of interest. In theory, the claimant’s lawyer has to protect his or her client’s interest and has to give the client candid advice on the virtues and vices of the funding proposal.²⁶⁹ However, in practice, it is possible that the claimant’s lawyer acts in his or her own interest and suggests funding regardless of the strength of the claim at hand because of the simple fact that funding equals guaranteed payment for the lawyer.

148. Furthermore, there is a legitimate concern that “an attorney’s primary loyalty will, as a practical matter, rest with the person or entity who pays him”²⁷⁰, bearing in mind that the funder is essentially the lawyer’s paymaster and that he or she is every so often selected or vetted by the funder before his or her appointment.²⁷¹ More generally, the funder always retains the ‘power of the purse’ (i.e. the power to discontinue further payments). This could result in the situation where the claimant’s lawyer will favour the funder’s interests due to purse strings rather than the interests of the claimant. This concern will arguably be the most pressing in situations where the funder has the right to choose the lawyer²⁷² and situations where the funder offers the prospect of repeat business for the lawyer.²⁷³
149. Furthermore, it is rather unlikely that the claimant’s lawyer will be in the best position to negotiate a good funding agreement with the funder, considering that the funder is the entity from whom the lawyer will receive compensation. An undesirable consequence could be that an unscrupulous funder might take advantage of its economic power, which it obtained by providing the indispensable funding, by insisting on unfair terms in a funding agreement, or even use its economic position to renegotiate terms to the detriment of the vulnerable client at a mature stage of the procedure. Due to the necessity of the funding for the continuation of the procedure and for the payment of the lawyer’s legal fees, a funded claimant – possibly on the advise of its lawyer – might then agree with these inequitable terms to avoid being forced to withdraw its claim. The latter is problematic because the claimant’s lawyer is obliged to ensure the proper protection of his or her client’s interests at all times.

150. There are of course some legal and non-legal factors that offer adequate protection against unfair terms. In the context of international commercial arbitration, many clients of funders are themselves experienced commercial parties who may have decided to obtain funding for their claim in order to appropriately manage the risks of pursuing the claim. Such clients with business acumen expect and demand professionalism from a funder and will ordinarily not be tricked into agreeing on unfair terms. Another self-evident factor that offers protection against unfair terms is the fact that there is competition among funders as well. They cannot afford to build up a lamentable reputation in the highly competitive market of TPF. Hence, funders will arguably prefer to agree on less attractive contract terms with the funded claimant, rather than losing business in the future. Finally, general contract law applies to all contracts, even if the contract in question is concluded to finance a dispute. Several doctrines, such as duress and good faith, protect the parties to a contract against unfair and


See for example the formal opinion issued by the Ethics Committee of the NYCBA in which it is stated that the lawyer and the client may face a conflict of interest when the lawyer is negotiating a financing agreement with the funder. NEW YORK CITY BAR ASSOCIATION, Formal opinion 2011-2: third party litigation financing, 2011, www.nycbar.org/ethics/ethics-opinions-local/2011-opinions/1159-formal-opinion-2011-02; see in the same sense, S. SEIDEL, “The lawyer’s “duty-to-know & duty-to-tell” in third party funding: a time to recognise & respect these obligations”, Corporate LiveWire 30 July 2012, 1-2 and www.fullbrookmanagement.com/2012/07/30/the-lawyers-duty-to-know-duty-to-tell-in-third-party-funding-a-time-to-recognise-respect-these-obligations/.


Supra 29-30, nos. 77-78.
abusive contractual provisions. However, an extensive comparative analysis of the respective national rules is required for this issue and this is beyond the scope of this thesis.

151. The following is another example of a possible conflict of interest that could occur in the event a party turns to TPF. Imagine the situation where parties go into settlement negotiations. The funder and the funded claimant might have divergent interest on this matter. The involvement – some might say intrusion – of a funder could discourage the feasibility of a possible settlement by the parties if it does not meet the funder’s expectations, despite being acceptable to the client. For instance, the funder might favour an early and cheap settlement in order to enhance its cash flow, whereas the claimant might prefer not giving in so easily and negotiate a more interesting settlement by dragging the negotiations out. Subsequently, a possible conflict of interest could arise – especially if the funder appointed the lawyer – because the lawyer may be incentivised to advise the claimant to accept the settlement, even where the settlement may not be in the claimant’s best interest. This could lead up to situations where the funder’s influence results in an abuse of process.

152. To the best knowledge of the author, there has not been an international commercial arbitration case that has dealt with this issue explicitly. However, the High Court of Australia addressed this issue in the Fostif case, in which the court ruled that the influence of the funder did not constitute an abuse of process and stated that it was unsurprising that a funder would want a certain control over the proceedings. Approximately simultaneously with the Fostif decision, the English Court of Appeal ruled in the Arkin case that the use of TPF could be upheld so long as the claimant would be the party in control of the conduct of the litigation and the party primarily interested in the result of the litigation. A clear distinction thus has to be made here with the Fostif decision where the funder could exercise a vast degree of control. The scope of the Arkin doctrine remains somewhat unclear, and it is uncertain whether the considerations that might make TPF permissible in casu (i.e. a competition claim), also apply, for instance, in an arbitral procedure.

153. Finally, the divergent interests between the funder and the funded party could also lead up to the stagnation of the proceedings in the event the relationship between the funder and the funded party becomes muddled. In other words, the effectiveness of the arbitral procedure is, due to the existence of a funding agreement, subjected to the cooperation and the good understanding between the funder and the funded party. For instance if the funder decides to stop paying the legal fees, the proceedings could be forced to stop.\footnote{See for example \textit{S\&T Oil Equipment \& Machinery Ltd. v. Romania}, ICSID Case No. ARB/07/13. In this case, an alleged misrepresentation led to the discontinuation of the proceedings because the funder stopped paying the procedural fees. For an in depth discussion of this case, see B. CREMADES, “Third party litigation funding: investing in arbitration”, 8(4) \textit{TDM} 2011, 25-32 and \url{www.curtis.com/siteFiles/Publications/TDM.pdf}. C. ROGERS, “Gamblers, Loan Sharks \& Third-Party Funders” in C. ROGERS, \textit{Ethics in International Arbitration}, Oxford University Press, forthcoming June 2014; A. CRIVELLARO, “Third-party funding and “mass” claims in investment arbitrations” in B. CREMADES and A. DIMOLITSA (eds.), \textit{Dossier X: Third-party Funding in International Arbitration}, Paris, ICC Publishing S.A., 2013, 144-145.}

C. \textit{How to avoid conflicts of interest from occurring?}

154. The participants at the Roundtable Discussions are convinced that in the event a conflict of interests occurs between the funder and the funded party, the attorney has to withdraw from the case.\footnote{M. SCHERER, A. GOLDSMITH and C. FLECHET, “Le financement par les tiers des procedures d’arbitrage international – une vue d’Europe Seconde partie: le debat juridique / Third Party Funding of International Arbitration Proceedings – A view from Europe Part II: The Legal Debate”, \textit{RDAI/IBLJ} 2012, 658.} This explains why some law firms are rather hesitant to accept cases in which their client is being funded.\footnote{Other law firms regard TPF as a welcoming option to finance their practice. See e.g. S. SEIDEL, “Maturing Nicely”, \textit{CDR} May 2012, \url{http://fulbrookmanagement.com/wp-content/uploads/2012/05/1May2012-Maturing-Nicelyb.pdf}.}

155. It is the author’s view that there are two other ways to avoid conflicts of interest with respect to the above-mentioned three-cornered relationship, namely: (i) drafting a funding agreement that deals with potential conflicts of interest; and (ii) having a disclosure obligation. This former will be discussed first.

156. CREMADES asserts that TPF implies a serious distortion of parties’ incentive in reaching an agreement since it is not only their interests at stake but also that of the funder.\footnote{B. CREMADES, “Third party funding in international arbitration”, \textit{Luzmenu} 2011, 5 and \url{www.luzmenu.com/cremades/Noticias/128/128.pdf}.} BOGART agrees with this and acknowledges that funded clients have to consider the economic implications of the funding agreement with respect to the amount of control the funder will have for instance when it comes down to a settlement.\footnote{C. BOGART, “Third party funding in international arbitration”, \textit{Burford Capital} 22 January 2013, \url{www.burfordcapital.com/articles/third-party-funding-in-international-arbitration/}.} BOGART also believes that a properly negotiated funding agreement does not make settlements more arduous because parties know at the outset of the proceedings that they will be given
up a part of the eventual settlement.\textsuperscript{287} The art thus lies in a proper funding agreement in which settlement provisions are clearly negotiated and agreed upon. As described above,\textsuperscript{288} the fact that a funder has agreed to fund a claim may noticeably increase the chance of the claim being settled at an early stage by agreement.

157. To avoid these kinds of conflicts of interest, the identification and management of potential conflicts should thus be addressed in the funding agreement. KHOURI, HURFORD and BOWMAN point out that the “the agreement should expressly recognise that the lawyer who has the conduct of the claim owes his or her professional and fiduciary duties to the claimant and that, in the event of a conflict of interest between the claimant and the funder, the lawyer may continue to act solely for the claimant, even if the funder’s interests are adversely affected by him or her doing so.”\textsuperscript{289}

158. Moreover, KHOURI, HURFORD and BOWMAN mention that the question of whether or not to settle can also be dealt with in the funding agreement. For instance, the following could be a provision in the funding agreement:

“Any irreconcilable difference over settlement must be referred to nominated counsel for a binding expert opinion on whether the settlement is a reasonable one, or the agreement may include some other form of dispute resolution clause to address this situation.”\textsuperscript{290}

159. It is thus crucial to have a properly drafted funding agreement, which deals with these issues. In doing so, one can avoid a possible deadlock situation if a conflict of interest occurs.

160. The second method to avoid conflicts of interest is a disclosure obligation. It is the author’s understanding that if the funder intervenes significantly in the proceedings, and if this involvement causes concern with respect to potential conflicts of interest, the funding agreement should automatically be disclosed to the arbitrators.\textsuperscript{291} This would allow the arbitrators to assess the,

\textsuperscript{288} Supra 27-29. nos. 73-76.
sometimes preponderant, role of the funder in the proceedings and his overall degree of involvement. As noted above,\(^{292}\) such a disclosure obligation, however, does not yet exist.

161. Finally, the Jackson Reforms\(^ {293}\) introduced cost consequences for failure to accept a settlement offer if the final judgment or award turns out to be lower than the settlement offer. Since the penalty is capped at GBP 75,000, it is unlikely to manifestly affect TPF settlements, considering that these tend to be much higher. Nevertheless, the idea of sanctioning the refusal of a decent settlement offer is extremely interesting. This could also be introduced in international arbitration, but the cap would have to be much higher in order to have some effect in practice.

2.1.2. Independence of arbitrators

A. General

162. Not only the claimant’s lawyer can cause conflicts of interest, but also the appointed arbitrator(s) because the involvement of a funder may raise the issue of impartiality or independence of the arbitrator(s) in certain circumstances. Several elements are amplifying the possibilities for arbitrator conflicts of interest: (i) the overall increase of funded cases;\(^ {294}\) (ii) the fact that the number of institutional funders that are funding international arbitration cases is still rather small; and (iii) the often close relations between elite law firms and leading arbitrators.\(^ {295}\)

163. The emergence of conflicts of interest during the proceedings can have catastrophic consequences because the parties may challenge the arbitrator’s independence at any stage of the arbitration,\(^ {296}\) which could result in the need to appoint a new arbitrator and this could disrupt the proceedings significantly, especially if this occurs in a later stage of the arbitration. Even more insidiously is when the conflict becomes known after the award has already been issued. The latter situation could result in the annulment or the denial of the recognition or enforcement of the award.\(^ {297}\)

\(^{292}\) Supra 53-54, nos. 135-137.


\(^{294}\) Supra 21-22, note 100.


\(^{296}\) See e.g. the following provisions in which the possibility of challenging an arbitrator is stipulated: art. 14(2) ICC Arbitration Rules, art. 8(1) ICDR Arbitration Rules, art. 10.4 LCIA Arbitration Rules; art. 13(1) UNCITRAL Arbitration Rules.

\(^{297}\) The New York Convention contains several grounds on which courts may invalidate or refuse to recognize the arbitral award when there are undisclosed conflicts of interest regarding the arbitrator(s). See for a discussion of these provisions, M. BRAVIN, “An Arbitrator’s Failure To Disclose Conflicts: Practical Advice Before Starting & After Completing An Arbitration”, Corporate Livewire 7 August 2012, www.corporatelivewire.com/top-story.html?id=an-arbitrators-failure-to-disclose-conflicts-practical-advice-before-starting-after-completing-an-arbitration.
Considering the sheer volume of the resources put into arbitral procedures, events like these are to be avoided at all costs. For these reasons, conflicts of interest should be addressed as soon as possible, preferably prior to the appointment of the arbitrator.

164. These two requirements diverge from each other in a subtle manner. Impartiality refers to the state of mind of the arbitrator and independence refers to previous or current relationships with other parties. The latter also encompasses relationships with funders to one of the parties in arbitration.

165. The independence and impartiality requirement of the arbitral tribunal is unquestionably one of the most fundamental principles in international arbitration due to the private nature of arbitration. Arbitral rules uniformly require the arbitrators to disclose information and circumstances that could scathe their independence, which is a clear indication of the importance of this principle in arbitration. Protecting these principles is therefore of paramount importance.

B. Potential conflicts of interest

166. The fact of the matter is that despite the general requirements of independence and impartiality of an arbitrator in arbitral rules, these rules do not sufficiently address this issue in light of the growth of the TPF practice. The presence of a funder can undeniably harm the independence of arbitrators and result in conflicts of interest because the appointed arbitrator(s) cannot check whether there is such a conflict.

167. The following are some examples of potential conflicts of interest in order to bestow the reader a better understanding of the problem that TPF might cause for the independence and impartiality of arbitrators. For instance, a situation could arise where a person acts as an arbitrator in a case in which the claimant is financed by the same funder who had also financed a claimant in another case in which the same person (i.e. the arbitrator) acted as that claimant’s counsel. Put differently, the same funder’s involvement in two cases with the same person acting in two different capacities (i.e. arbitrator and counsel), does not sit well with respect to the impartiality and independence of the latter.


301 With regard to arbitral proceedings conducted under the ICC, ICDR or LCIA Arbitration Rules, prospective arbitrators have the obligation to disclose information about their independence to respectively the ICC Secretariat (art. 11(2) ICC Arbitration Rules), the ICDR administrator (art. 7(1) ICDR Arbitration Rules), or the LCIA Registrar (art. 5.3 LCIA Arbitration Rules).
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hence causing conflict of interests.\textsuperscript{302} This concern is particularly fitting for international arbitration, considering that counsel and arbitrators are often drawn from essentially the same pool since the arbitration circuit is such a close-knit industry where “everyone knows everyone.”\textsuperscript{303}

168. Furthermore, it is possible that the funder has the power to appoint the arbitrator. In the latter situation, it is practically self-evident that the funder would turn to arbitrators with whom it had prior commercial relationships and contacts. Such a situation could only increase the doubts with respect to the arbitrator’s independence and impartiality.

169. There are some other examples of situations which could lead to conflicts of interest: (i) multiple appointments of the same arbitrator by the same funder;\textsuperscript{304} (ii) an existing relationship between the funder and the arbitrator’s law firm; and (iii) shares held by the arbitrator in the funding corporation.\textsuperscript{305}

170. To avoid potential conflicts of interest in situations of ‘repeat appointments’ of the same arbitrator by the same funder,\textsuperscript{306} the International Bar Association’s Guidelines on Conflict of Interest in International Arbitration (“IBA Guidelines”)\textsuperscript{307} require disclosure of these ‘repeat appointments’ if

\begin{itemize}
  \item \textsuperscript{304} Commonly referred to as “repeat appointments” by commentators. See e.g. C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, Ethics in International Arbitration, Oxford University Press, forthcoming June 2014.
  \item \textsuperscript{306} See for instance OPIC Karimum Corporation v. The Bolivarian Republic of Venezuela, ICSID Case No. ARB/10/14 (May 5, 2011), in which the tribunal stated that multiple appointments might affect an arbitrator’s ability to exercise independent judgment; see for a discussion on this case, S. MENON, “Some Cautionary Notes for an Age of Opportunity”, Chartered Institute of Arbitrators International Arbitration Conference 22 August 2013, 14-15 and www.singaporelaw.sg/slaw/images/media/130822%20Some%20cautionary%20notes%20for%20an%20age%20of%20opportunity.pdf.
  \item \textsuperscript{307} Available at www.ibanet.org/Publications/publications_IBA_guides_and_free_materials.aspx#conflictsofinterest.
\end{itemize}
the arbitrator in question has had more than two appointments in the last three years by the same party, and three or more appointments in the last three years by the same law firm. However, the current IBA Guidelines contain no provisions in which TPF is mentioned expressly because they were written before the advent of TPF. This could change in the near future because a sub-committee of the IBA Task Force responsible for the IBA Guidelines has been constituted and is considering whether the IBA Guidelines require modifications in light of recent developments, such as TPF.

C. Current applicable rules

171. Let us now take a look at the current applicable rules regarding an arbitrator’s independence and the disclosure of conflicts of interest when an arbitration is conducted under the auspices of the ICC, the ICDR, or the LCIA or when the arbitration is conducted on an ad hoc basis.

172. The arbitral rules use different standards to determine what information and circumstances should be disclosed. The UNICTRAL Arbitration Rules provide that the arbitrator must disclose all circumstances “likely to give rise to justifiable doubts as to his or her impartiality or independence.” The LCIA Arbitration Rules provide in similar fashion that the arbitrator shall disclose circumstances “likely to give rise to any justified doubts as to his impartiality or independence.” The ICDR Arbitration Rules similarly require the disclosure of “any circumstance likely to give rise to justifiable doubts.” The ICC Arbitration Rules require disclosure of “any facts or circumstances which might be of such a nature as to call into question the arbitrator’s independence in the eyes of the parties.”

173. Lastly, the IBA Guidelines likewise provide that the arbitrator must disclose circumstances that “may, in the eyes of the parties, give rise to doubts as to the arbitrator’s impartiality or independence.” Therefore, in theory, arbitrators have to disclose the pertinent information regarding the TPF relationship if one of the parties is receiving funding.

308 IBA Guidelines 3.1.3.
309 IBA Guidelines 3.3.7.
311 Art. 11 UNCITRAL Arbitration Rules.
312 Art. 5.3 LCIA Arbitration Rules.
313 Art. 7 ICDR Arbitration Rules.
314 Art. 11(2) ICC Arbitration Rules.
315 General Standard 3(a) IBA Guidelines.
174. However, an arbitral tribunal can only properly exercise control over funded proceedings if it is aware of the existence of the funding in the first place. There are no rules that specifically require a party to disclose its funding relationship and many arbitrators and lawyers are discussing whether such an obligation should be introduced. Moreover, as said, funding agreements often contain a confidentiality clause, which results in the situation where arbitrators rarely know if a party is being funded.

175. Although the institutional arbitration rules require the arbitrator to be independent, the question of how to interpret independence remains unanswered because none of the above-mentioned rules defined the concept. The IBA Guidelines were created with the purpose of tackling this problem by providing lists of specific circumstances that may give rise to questions about an arbitrator’s independence and impartiality and these circumstances have to be disclosed by the arbitrator.

176. Several provisions of the IBA Guidelines provide that arbitrators should disclose their past or present relationships with the parties to the dispute and the law firms representing the parties. Furthermore, the arbitrator can also have a financial conflict with respect to the arbitration. Subsequently, the question of which corporate interests should be disclosed in international arbitration rises. The IBA Guidelines provide us with the following answer: only a “significant financial interest” in the outcome of an arbitration can form the basis for an arbitrator to have a financial conflict. BOGART notes that the funding of a claim would not create such a financial interest unless the arbitrator and the funder were the same person.

177. BOGART points out the following hypothesis that could cause a conflict of interest, namely the situation where a funder is financing the action before the arbitrator and simultaneously is funding a separate matter in which the arbitrator’s firm is counsel. According to BOGART this is clearly not a conflict of interest because under the IBA Guidelines, only parties and their affiliates can create

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317 Supra 50, no. 126.
318 See e.g. IBA Guidelines 3.1.4, 3.3.3, 3.4.2.
319 See general standard 2(d) IBA Guidelines; this standard is not as clear as the one provided by the USSC (supra 53, no. 135).
321 See for the definition of affiliate footnote 5 of the IBA Guidelines.
such conflicts and funders are, under the law of any common law country, not affiliates, nor are funders affiliates under the definition of an affiliate in the IBA guidelines.

178. TRUSZ does not share BOGART’s opinion and states that funders become an affiliate of the funded party due to the power the funder subsequently receives to control the party’s dispute. Assuming that the funder would be qualified as an affiliate of the funded client, the arbitrator would subsequently be subject to a disclosure obligation of several circumstances that are enumerated in the IBA Guidelines. It is clear that this issue is not yet settled and ambiguity still exists. However, it can and should be noted that the IBA Guidelines expressly state that any doubt as to whether an arbitrator should disclose should be resolved in favour of disclosure. This author thus recommends arbitrators to disclose the respective information as long as this issue is not settled.

179. However, this author cannot emphasize enough, that regardless of this discussion on the qualification of funders as affiliates, the current arbitral rules and IBA Guidelines will have no effect on TPF relationships in practice as long as the arbitrator does not know of the existence of the funding agreement. It is therefore crucial for the arbitral tribunals to be informed about the existence of TPF from the outset, in order to be in a proper position to assess possible conflicts of interest resulting from TPF relationships.

D. How to avoid conflicts of interest from occurring?

180. The end result of the above-mentioned different standards is a lack of consistency and certainty among arbitrators regarding both the scope of an arbitrator’s disclosure obligations and the

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322 The term ‘affiliate’ often has different definitions in various jurisdictions. See generally C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, Ethics in International Arbitration, Oxford University Press, forthcoming June 2014.


324 J. TRUSZ, “Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration”, Geo. L. J. 2013, 1670; Black’s Law Dictionary 67 (9th ed. 2009) defines affiliate as “a corporation that is related to another corporation by shareholdings or other means of control”; for a more in depth discussion on whether funders can be qualified as affiliates, this author recommends the reader to consult C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, Ethics in International Arbitration, Oxford University Press, forthcoming June 2014.

325 See, for example, IBA Guidelines 2.3.6: “The arbitrator’s law firm currently has a significant commercial relationship with one of the parties or an affiliate of one of the parties”; for more information on the IBA Guidelines and more examples of how the funder as an affiliate could be implicated by several circumstances mentioned in the IBA Guidelines, see J. TRUSZ, “Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration”, Geo. L. J. 2013, 1670-1673.

326 General Standard 3(c) IBA Guidelines.

due diligence obligations in case of potential conflicts of interest.\textsuperscript{328} It is the author’s view that some of the conflicts of interest could be avoided if there was more certainty by developing and introducing a uniform code of conduct for arbitrators. However, the feasibility of such a uniform code seems questionable considering the highly competitive market between the arbitral institutions. The author therefore poses the rhetorical question whether there would be willingness among these institutions to develop such a code.

181. In short, the author feels that the only efficient way to avoid these kinds of conflicts of interest is by introducing a disclosure obligation for TPF agreements.

2.2. Disclosure obligation to decide on allocation of costs or security for costs

182. TPF has a strong chance of influencing the costs of the arbitration proceedings at several stages of the proceedings: (i) at any time during the course of the proceedings when the arbitral tribunal decides on security for costs; and (ii) at the time of the final decision by the arbitral tribunal regarding the allocation of the arbitration fees. As noted above,\textsuperscript{329} TPF relationships are inclined to remain confidential because funders prefer to keep the funding relationship, which can be deduced from the fact that most funding agreements contain confidentiality clauses.

183. The question whether TPF agreements should be considered by the arbitral tribunal when deciding on the allocation of costs or security for costs should therefore be discussed together with the discussion on whether to create a disclosure obligation or not. Even if tribunals should indeed take funding relationships into account, this rule would remain dead letter if the tribunals would remain unaware of the existence and identity of the funder.

184. After an introduction on how arbitral tribunals decide on the allocation of costs and security for costs in international arbitration in general, this section set forth the opposing views expressed by funders, commentators and arbitrators regarding taking TPF agreements into account by the tribunal when making such decision. This section concludes with the author’s view on the most apt approach towards allocation of costs and security for costs when TPF is involved.


\textsuperscript{329} Supra 50, no. 126.
2.2.1. Allocation of costs in international arbitration

185. The allocation of costs in international arbitration is generally decided by the arbitral tribunal, who has a broad discretion on the issue, unless the arbitration rules or the parties’ agreement state otherwise.\(^{330}\) \(^{\text{SCHERER}}\) explains how arbitral tribunals decide on adversary’s costs in practice:

> “While there are no express international standards, and although the “costs follow the event” rule whereby the losing party pays for its adversary’s costs is not universally accepted, tribunals often allow the prevailing party to recover reasonable costs from the losing party.”\(^{331}\)

186. Arbitral tribunals thus generally have a broad discretion for decisions about cost shifting, and there does not seem to be any clear coherent system or procedure in this respect.\(^{332}\) In practice, three different cost allocation schemes that are used by arbitral tribunals can be distinguished: (i) the ‘cost follow the event’ principle (“English rule”);\(^{333}\) (ii) the ‘pay your own’ approach (“American rule”);\(^{334}\) and (iii) the ‘factor dependent’ approach.\(^{335}\)

187. The ‘English rule’ implies that the unsuccessful party will be ordered to pay the cost of the successful party.\(^{336}\) A key objective of this rule is preventing frivolous arbitral procedures.\(^{337}\)

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\(^{333}\) See Civil Procedure Rules, rule 44.2(2)(a) for litigation and Arbitration Act 1996, sec. 61(2) for Arbitration in England.

\(^{334}\) In France, parties usually bear their own legal costs too, despite the fact that art. 700 of the French Code de Procédure Civile grants judges the power to order the unsuccessful party to pay the successful party’s legal costs. See generally W. KIRTLEY and K. WIEZRYKOWSKI, “Should an Arbitral Tribunal Order Security for Costs When an Impecunious Claimant Is Relying upon Third-Party Funding?”, 30(1) \textit{J. Int. Arb.} 2013, 19.


\(^{337}\) Several commentators believe that potential liability for adverse costs filters out unmeritorious claims. See e.g. C. VELJANOVSKI, “Third-Party Litigation Funding in Europe”, 8 \textit{J.L. Econ. & Pol’y} 2012, 443; R. HARFOUCHE, and J. SEARBY, “Third-Party Funding: Incentives and Outcomes”, \textit{Global Arb. Rev.} 2013, 10; U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, \textit{Third Party Financing: Ethical & Legal Ramifications in Collective
However, in the event the parties did not agree on how to costs should be allocated, then the arbitral tribunal will still have discretion, making it unsure which rule they will apply and therefore leaving the door open for frivolous claims. In order for this objective to become truly effective, parties should have the certainty that the ‘English rule’ will apply.

188. The ‘American rule’ implies that both parties will be responsible for their own expenses and the costs related to the procedure will be split evenly between the parties. Arbitral tribunals can adopt this rule and still deviate from it in situations such as bad faith of where the case turned out to be a frivolous one.

189. The ‘factor dependent’ approach implies that both parties are liable for the costs based on the level of success. If for instance the claimant’s claim is not entirely successful on all issues, then the tribunal could decide that some of the costs should be covered by the respondent.

190. There is now a tendency for arbitral tribunals to move away from the ‘American rule’ and more towards the ‘English rule’. The arbitral tribunals now prefer an approach where they take the specific circumstances and facts of the case into consideration. This approach can be qualified as the middle road between the ‘American rule’ and the ‘English rule’. The Thunderbird Gaming case is a good example of this approach. In this case, the claimant had to pay the costs of the respondent state because the tribunal ruled that certain claims were frivolous and that the proceedings were conducted in bad faith.

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2.2.2. Security for costs in international arbitration

191. Considering the significant costs, which international arbitral proceedings entail, and the possibility of cost shifting in arbitration due to the discretionary power of the arbitral tribunals to allocate costs, it is every so often recommended to order security for costs in order to ensure the succeeding party (claimant or respondent) that it can recover its costs.\smallskip

192. An arbitral tribunal may order the payment of security for costs during the course of the proceedings. Let us assume, for the sake of argument, that tribunals will consider TPF agreement when deciding on security for costs. The tribunals will thus be able to order security for costs during the proceedings and not only at the outset, but also for instance after they have learned of the existence of the TPF relationship.

193. Despite the tool of security for costs not being universally accepted, it is nevertheless gradually getting traction to become common practice in international arbitration proceedings.\footnote{344}{See generally M. Scherer, “Out in the open? Third-party funding in arbitration”, CDR 2012, 56-57 and www.cdr-news.com/categories/expert-views/out-in-the-open-third-party-funding-in-arbitration; J. Waincymer, Procedure and Evidence in International Arbitration, Alphen aan den Rijn, Kluwer Law International, 2012, 641.} However, security for costs is not always available. It depends on the possible agreement of the parties on that subject,\footnote{345}{Especially civil law jurisdictions are unfamiliar with security for costs. Providing security for costs is considered to be a typically English legal mechanism. See generally W. Kirtley and K. Wietrzykowski, “Should an Arbitral Tribunal Order Security for Costs When an Impecunious Claimant Is Relying upon Third-Party Funding?”, 30(1) J. Int. Arb. 2013, 19.} the applicable arbitral rules or the national laws at the seat of arbitration.\footnote{346}{Some funders, such as Harbour Litigation Funding and IMF, offer security for costs to their clients as part of the funding package. See generally W. Kirtley and K. Wietrzykowski, “Should an Arbitral Tribunal Order Security for Costs When an Impecunious Claimant Is Relying upon Third-Party Funding?”, 30(1) J. Int. Arb. 2013, 17.} The ICC, LCIA, ICDR, and UNCITRAL Arbitration Rules each contain a provision giving the arbitral tribunal the authority to order security for costs.\footnote{347}{J. Waincymer, Procedure and Evidence in International Arbitration, Alphen aan den Rijn, Kluwer Law International, 2012, 621-622.} Tribunals ordinarily order security for costs if: (i) the requesting party shows that it has a solid chance of succeeding on the merits; and (ii) that the opposing party does not possess sufficient financial means to satisfy a potential future adverse costs

\footnote{348}{Art. 28(1) ICC Arbitration Rules; art. 25.1 LCIA Arbitration Rules; art. 21 ICDR Arbitration Rules; art. 26 UNCITRAL Arbitration Rules.}
The arbitral tribunal will also consider if bad faith was involved in the party’s actions when determining to grant security for costs.\textsuperscript{350}

\section*{2.2.3. Should the arbitral tribunal take funding agreements into account when deciding on the allocation of costs and security for costs?}

\subsection*{A. General}

TPF in arbitration can give rise to a considerable number of issues regarding the costs of the arbitration. Let us imagine the situation where a party, who does not have the financial resources to pay any adverse costs in the event its claim is unsuccessful, initiates a claim in arbitration after obtaining the necessary funding. It is rather unlikely in such a case that the prevailing party will recover its costs from the funded party who lost. Moreover, it is equally unlikely that the prevailing party will be able to recover its costs from the funder because a funder is not a party to the action, nor does the funder (generally)\textsuperscript{351} control the proceedings.\textsuperscript{352} Some funding agreements nevertheless expressly state that the funder is not liable for adverse costs to nip any debate on the issue in the bud.\textsuperscript{353}

The moot point is whether TPF agreements should and could be taken into account by the arbitral tribunal when determining to grant the requested security for costs or when deciding on the allocation of costs. Two divergent views can be identified among commentators on this issue. The following section will first discuss the critics of the taking into account of TPF agreements for decisions on costs by arbitral tribunals. Subsequently, the view of the proponents will be discussed regarding this issue.


\textsuperscript{351} Supra 55-57, nos. 143-146.


B. Critics

196. Some commentators assert that not considering TPF when deciding on security for costs is logical, since TPF has already been decreed on previous occasions as an element to determine the awards of costs. Recent international investment arbitration cases confirm that TPF agreements should not be taken into account when deciding on the allocation of costs. For instance in the recent Kardassopoulos v. Georgia case, Georgia reasoned that because Kardassopoulos was being funded by a third-party, they should not have to bear his costs of the arbitral proceedings. The arbitral tribunal subsequently noted that it found "no principle why any such third party financing arrangement should be taken into consideration in determining the amount of recovery by the Claimants of their costs."

197. Leading arbitrators, such as Van den Berg, and several commentators concur with the decision to not take TPF into account when allocating costs between parties. Allowing TPF to be considered for either awards of costs or security for costs would indeed cause some uncertainty among the parties involved in the arbitration. Furthermore, there is an inherent risk of stifling meritorious claims if a tribunal would order the financially distressed claimant to provide security for costs based on the simple fact that he or she is being funded because if the funder refuses to cover these costs, the claimholder would be compelled to stop the arbitral proceedings. For instance in the Hamester case, the arbitral tribunal refused to grant security for costs because this could potentially stifle the claim due to the fact that the claimant relied on external funding.


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198. There is also a risk of delaying the proceedings if arbitral tribunals would routinely take TPF into account when considering granting security for costs, because it is not unlikely that the opposing party would almost automatically apply for security once it would become aware that its adversary is being funded. TPF also raises the question regarding the possibility for the funded party to recover the incurred costs. If the funder paid for all of the funded party’s attorney fees and all other costs, who then should be considered to have incurred the costs in question? The client does not suffer any loss as such because the funder covers all the costs.

199. Furthermore, the issue remains that the funder is not a party in the arbitration. It is undeniably questionable if a different treatment with regard to security for costs between claimants relying on TPF and claimants using other funding models can be justified because TPF is fundamentally not different from other types of funding. It appears that the use of other funding models to finance a claim have not been taken into account when determining security for cost. Hence, it is the author’s view that claimants should arguably not be treated differently for the sole reason that he or she chose to rely on TPF in lieu of on another type of funding.

200. Moreover, funders may be more reluctant to disclose the TPF relationship if they know at the outset of the proceedings that the relationship could be considered for determining security for costs. By doing so, potential conflicts of interest will remain unknown. It is the author’s view that the necessity of preventing conflicts of interest should be given more weight than eliminating funding relationships from determining security for costs. Put differently, if the funders would have guarantees that the funding relationship would not be taken into account by the tribunal when deciding on allocation of costs or security for costs, they could be more incentivised to disclose the relationship and thus making it possible to address potential conflicts of interest.

201. Finally, the pivotal and ostensibly insurmountable obstacle impeding arbitral tribunals from considering TPF for awards on costs is the lack of jurisdiction of the tribunal to order the funder to pay adverse costs because the funder is not a party in the arbitration. Put differently, the arbitrators

359 Supra 6-15, nos. 17-46.
361 This argument is repeated and explained in more detail further on when discussing the proposal for a disclosure obligation (infra 90-91, nos. 245-247).
cannot address the TPF agreement because the funding agreement is alien to the legal relations between the claimant and the respondent and the arbitrator is only competent with respect to these parties. In general, the arbitral tribunal thus lacks the required jurisdiction to order the funder to pay any adverse costs, save for instances where the arbitration agreement is considered to be extended (e.g., under available theories, such as implied consent) or de facto assigned to the funder (e.g., if a company buys the claim, award, or the company who initiated the claim).363 The only leverage that tribunals have to ensure contributions form the funders appear to be at the security for costs stage.

C. Proponents

202. Other commentators champion the taking into account of TPF for decision on allocation of costs and security for costs. Their main concern is that claimants, who lack sufficient available finances for the arbitration, would abuse the system via TPF because he or she would gain from succeeding in the arbitration, but would be unable to pay for costs if the claim is unsuccessful. Put differently, this could create a ‘moral hazard’ because the party can only gain from the proceedings. KALICKI describes this scenario as the “arbitral hit and run” and explains that “security for costs is more likely to be awarded where the claimant’s arbitration fees and expenses are being covered by a related entity or individual who stands to gain if the claimant wins, but would not be liable to meet any award of costs that might be made against the claimant if it lost.”364 To mitigate the exposure to this risk, CRIVELLARO suggests that “the existence of third-party funding, its conditions, and the

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identity and solvency of the third-party funder should be disclosed when arbitration proceedings commence.”

203. Although this thesis has argued that it is unlikely that TPF would foster frivolous claims, this is nevertheless a legitimate concern expressed by several commentators. A TPF relationship can indeed be an indication that the party has insufficient financial recourses for the arbitration and some argue that the relationship should therefore be disclosed to give the arbitral tribunal the opportunity to consider it for security for costs.

204. Furthermore, arbitral tribunals customarily require, besides being in a precarious financial situation, a fundamental change in circumstances to order security for costs. The reasoning behind this is that the party requesting security for costs knew of the financial situation of its adversary when they entered into the business relationship, regardless of the TPF agreement. Nevertheless, it is the author’s opinion, as is it KIRTLEY and WIEczRZYKOWSKI’s view, that ordering security for costs can and should be justified to protect respondents from spurious claims when TPF is used abusively. It remains to be seen whether arbitral tribunals will adopt this line of reasoning.

205. Who then would have to bear the risk of having to pay security for costs or adverse costs awards: the funded client or the funder? It is possible, if not probable, that the client and the funder agree on a maximum adverse costs award that the funder would have to pay if the client loses the case. However, most funders are reluctant to assume liability for adverse costs awards since they already bear a vast amount of financial risk. There is nonetheless a possibility that funders may find themselves liable to provide security for costs and LAMM and HELLBECK reason that the risk is greater

366 Supra 31-32, nos. 80-81.
372 Nonetheless, some funders, such as IMF, expressly state that they offer payment of any adverse costs as a part of the funding package. See W. KIRTLEY and K. WIEczRZYKOWSKI, “Should an Arbitral Tribunal Order Security for Costs When an Impecunious Claimant Is Relying upon Third-Party Funding?”, 30(1) J. Int. Arb. 2013, 18.
when the so-called ‘English rule’ applies. An illustrative example of this issue is the Arkin case, in which the Court ruled that the funder was liable for all costs up to the amount of its contribution to the litigation because justice would be better served if costs could be recovered from the funder whose financing permitted a claim, that proved to be without merit, to be pursued.

Furthermore, if the client would be ordered to pay security for costs due to the presence of TPF, the principle of access to justice could be harmed. Let me explain. By increasing the financial risk on the funding company, the likelihood that the funding agreement would be terminated would also increase. Assuming that TPF will most often be used by parties with insufficient financial funds, increasing the probability of the termination of the funding agreement or the dismissal of the claim because the party did not comply with the order, could thus decrease the access to justice. This is problematic especially considering that the original intention for the introduction of TPF was to increase the access to justice.

Arbitrators thus have the task to undertake a delicate balancing exercise between the right of the claimant of access to justice and the protection of the respondent for the incurred costs.

Given the sensitivity of this balancing exercise, the circumstances that could justify an order for security for costs should therefore be strictly limited. A ‘blanket approach’, as KIRTLEY and WIE TRZYKOWSKI call it, whereby security for costs would be automatically ordered if TPF is involved, would create an inequitable distinction between claimants with meritorious claims who relied on TPF rather than on alternative types of financing.

373 Supra 70-71, no. 187.
375 Supra 26-27, no. 71.
378 Supra 25-27, nos. 67-72.
381 Supra 6-15, nos. 17-46.
208. **DE BRABANDERE** and **LEPELTAK** also argue in favour of considering TPF agreements for the purpose of deciding on the allocation of costs or security for costs. They note that the decisive factor will be the level of influence of the funder on the proceedings and the costs. Therefore, they suggest that tribunals should make a distinction between cases in which funders had a preponderant influence on the proceedings and cases where the funder only had a marginal influence. The tribunal could then, if the interference had a negative influence on the proceedings, for instance by delaying the proceedings, take the TPF agreement into account when considering the allocation of costs. 382

209. There is some case law from local courts in the U.S. and in England383 in which the courts ruled that the responsibility of the funder should be extended to pay for the successful adverse party’s litigation costs. For instance in *Abu-Ghazaleh v. Chaul*, the District Court of Appeal of Florida concluded that the funders were parties to the lawsuit because they had the control to direct the course of the proceedings and were therefore liable for the victorious defendant’s fees and costs. 384 It is clear that a consensus does not yet exist about taking the TPF into account for ordering security for costs or for the allocation of costs.

210. Those in favour of considering TPF agreement for awards on costs have to realize that the main concern is the opacity of TPF agreements. If the funding relationship should be taken into account, then a disclosure obligation would have to be imposed at the outset of the arbitration.385

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383 In *Dymocks Franchise Systems (NSW) Pty Ltd. v. Todd* (Costs), [2004], 1 W.L.R. 2807, the Court made the distinction between ‘pure’ funders and funders who had substantial control over the proceedings. The Court found that justice requires that the funder would pay the successful party’s costs if the proceedings fail if the funder had substantial control. ‘Pure funders’ will generally not have to carry the awarded costs. In the *Arkin* case, the Court ruled that the funder had to pay the successful party’s adverse costs to the extent of the amount funded (supra 26-27, no. 71).


385 It is also possible that the respondent or the tribunal becomes aware of the fact that the claimant is being funded, absent a disclosure obligation, for instance in the event of a leak. See on the issue of timing of disclosure of TPF and the impact on ICSID jurisdiction, the recent case of *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1 (decision on jurisdiction, 21 December 2012, paras. 239-259). A. MEYA, “Third-party funding in international investment arbitration” in...
However, as already indicated several times, the leading arbitral institutions do not have any rules to date, which require a party to disclose if it is being funded.386

211. Such an obligation could give the tribunal the opportunity to assess whether it has to order the funded party to provide security for costs and whether it should take the funding agreement into account when allocating the costs. For example, if the tribunal finds out that the funded party could not participate in the arbitration without the funding agreement, it could subsequently order security for costs in order to ensure that the funded party would be able to pay a future adverse costs award. A funding agreement, however, may not automatically lead to the tribunal ordering security for costs because, as noted above, it might well be that the funded party turned to TPF for reasons other than being impecunious.387

212. Despite the sound reasons for arguing that TPF should be taken into account, the fact of the matter is that no publicly available case has ruled in favour of this view yet, leaving the discussion wide open.

2.3. Giving arbitral tribunals the opportunity to assess the need to impose a duty of confidentiality on funders

213. Confidentiality in international commercial and investment arbitration is a topic from which much debate has sprung. After briefly discussing confidentiality in international arbitration as such, this section will examine the impact that the presence of a funder could or even should have on the confidential nature of international arbitration.

2.3.1. Confidentiality in international arbitration

214. In short, arbitration proceedings are confidential if the parties in arbitration made an agreement hereof, by either selecting arbitration rules with explicit provisions thereof, or under domestic statutory regulations.388 However, only few national laws389 regulate confidentiality in

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386 Supra 53-54, nos. 135-137.
387 For instance, if the funded party uses TFP because it wants to manage his risks or facilitate his cash flow (supra 29-30, nos. 77-78).
389 Worldwide, there are only a few countries that expressly address the confidentiality of the arbitral process, countries such as New Zealand, Norway, Spain, Romania, Peru and the Philippines. See for a discussion, I. SMEUREANU, “Confidentiality in arbitration revisited: protective orders in the Philippines”, Kluwer Arbitration
arbitration since a sizeable number of countries have adapted the UNCITRAL Model Law, whose drafters made it clear that “confidentiality may be left to the agreement of the parties or the arbitration rules chosen by the parties.”

215. For instance, in article 22(3) of the ICC Arbitration Rules it is determined that “upon the request of any party, the arbitral tribunal may make orders concerning the confidentiality of the arbitration proceedings or of any other matters in connection with the arbitration and may take measures for protecting trade secrets and confidential information.” The parties thus have to explicitly request confidentiality orders because the tribunal does not have the discretionary power to do so.

### 2.3.2. Are third-party funders bound by a duty of confidentiality?

216. For the sake of argument and to facilitate further debate on the possible influence of the presence of a funder on the confidentiality of arbitration, let us assume that a duty of confidentiality exists and that this duty falls first on the parties to the arbitration and their respective counsel.

217. As for the question whether funders who participate in international arbitration are bound by a duty of confidentiality, two different approaches can be identified. First, the funder may be considered to be part of the funded party. In that capacity, the funder will be in principle held to the same duty of confidentiality as the parties. Second, the funder may be treated like any other third party in arbitration. This implies that the funders will be bound by a duty of confidentiality, only if they expressly sign a promise of confidentiality, as is the practice for third parties in international arbitration. Until this discussion is settled, it is recommended that the arbitral tribunal asks the funders to sign a confidentiality agreement in order to avoid later complications.

218. This discussion may seem purely theoretical considering that a disclosure obligation is not yet in existence for TPF agreements. The arbitral tribunals will most often not be aware of the fact that one of the parties is being funded, hence it will not be able to assess the question whether it is

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390 Belgium is one of the latest countries to adapt its Arbitration Act, which is now based on the UNCITRAL Model Law. The new Act entered into force on 1 September 2013. Wet 24 juni 2013 tot wijziging van het zesde deel van het Gerechtelijk Wetboek betreffende de arbitrage, BS 28 juni 2013, 41.263; see also H. VERBIST, “New CEPANI rules of Arbitration in force as from 1 January 2013”, *Tijdschrift@iapr.be* 2012, www.ipr.be, 51-60.


392 See in the same sense, art. 30 LCIA Arbitration Rules and art. 34 ICDR Arbitration Rules.

necessary to ask the funder to sign a promise of confidentiality. A possible solution would be for the tribunal to systematically ask the parties if they are being funded.

3. Feasibility of a disclosure obligation

3.1. Issues with establishing a disclosure obligation

219. Such a disclosure obligation will be challenging to establish and implement in practice because of several issues, such as the cumbersome hurdle of defining TPF agreements and what would fall within the ambit of such an obligation. As explained above, one could go for a broad definition of TPF *(i.e. TPF sensu lato)*, such as any financial solution offered to a party regarding the funding of proceedings in a given case. Such a definition covers all kinds of funding agreements, such as lawyers’ contingency fees or LEI. If such a broad definition were used to determine the funding agreements that require disclosure, then all of these situations would have to be disclosed.

220. One could also narrow the definition by adding certain requirements, such as requiring that the funder has to be a third party to the proceedings (thus excluding attorney financing); or that the funder has to be a professional (thus excluding *ad hoc* solutions like borrowing money from a relative); or that the funder is entitled to a percentage of the award or a cost multiple (thus excluding LEI).

221. The question remains why such narrowly defined TPF agreements should be subject to mandatory disclosure requirements, whereas other types of funding, which fall within the ambits of TPF *sensu lato*, should not be disclosed. The reasons that could justify a mandatory disclosure apply not only for TPF *sensu stricto* but also TPF *sensu lato*. For example, the concerns about liability for adverse costs may be equally justified if the claimant has recourse to a contingency fee arrangement or an ATE insurance arrangement. The same goes for conflicts of interest. Imagine the situation where a presiding arbitrator in an arbitral procedure, in which one of the parties is funded by an insurer, is at the same time counsel for a client, who is insured by that same insurer, in another case. Such situations could result in conflicts of interest. In short, one has to determine which situations in international arbitration proceedings should be subject to disclosure obligations and here rests the real struggle of this issue.

394 *Supra* 6-15, nos. 17-46.
396 *Supra* 72-73, nos. 191-193.
222. Let us assume for a moment the hypothesis that there is a disclosure obligation. Further questions still remain as to the modalities of such an obligation; questions such as, should only the existence of a TPF agreement, or the actual contents of the TPF agreement be disclosed and should the TPF agreement be disclosed to only the arbitral tribunal or to all the parties involved in the arbitration? As for the former question, the author deems it likely that the funders will be reluctant to disclose the exact terms of the funding agreement, especially considering that currently the common practice is to keep the funding agreement in its entirety confidential. As for the latter question, disclosure to the tribunal might be sufficient, considering that the tribunal will be the ultimate decision maker and considering the reasons that could justify a disclosure obligation (i.e. to assess the necessity for security for costs and to avoid conflicts of interest).

223. CREMADES believes that arbitration is becoming increasingly transparent with a greater interaction between the parties and the arbitral tribunal. The author agrees with CREMADES, but only with respect to investment arbitration. International investment arbitration necessitates certain procedural transparency, whereas such transparency is generally not required in the private and confidential world of international commercial arbitration. A good illustration is the fact that the UNCITRAL has been working on new transparency rules for investment arbitration. The public nature of these proceedings is desirable since one of the parties is a sovereign state who has the duty to inform its parliament and citizens of potential liabilities, such as losing in arbitration. For this particular reason, it is of paramount importance to determine who the funder behind the official claimant is. DE BRABANDERE states that it is unlikely that the new transparency rules will result in a substantive diminution of parties going to arbitration and that practice is proving this. Thus, in view of the transparency of arbitral proceedings in international investment disputes, it may be argued that a disclosure obligation of TPF agreements is even more pressing in investment arbitration than in international commercial arbitration.

224. For now, there are no signs that denote the same evolution in international commercial arbitration. There is no need for publicity as in investment arbitration where this is favourable because one of the parties is a state.

399 Question asked to professor DE BRABANDERE on 15 May 2013.
3.2. Funders’ perspective on disclosure

225. To discuss the funders’ perspective, the author mainly relies on three recent conferences on TPF where several funders were present, namely the above-mentioned Roundtable Discussions and the ICC Institute of World Business Law’s 32nd annual meeting held in Paris on 26 November 2012 (“ICC Meeting”).

226. Funders are in general reluctant to disclose, if not their involvement as such, then at least the funding agreements, absent situations where the client is obliged to do so under an applicable legal disclosure obligation or if particular situations justify such disclosure, such as a possible conflict of interest. Among the participants to the Roundtable Discussions, there was a clear predilection for non-disclosure of the funding agreements, due to the suspicion that disclosure could adversely influence a tribunal.

227. At the ICC Meeting, the TPF corporations present were also not in favour of an extensive disclosure of the terms and conditions of the funding agreement because many confidentiality rules apply for various reasons – including the sensitive nature of information – and in their view no question of mandatory disclosure should arise, let alone the fact that there do not exist, to date, any rules on the international level that require such disclosure. As said before, the funders guard themselves against the disclosure of the funding agreements by using confidentiality agreements or by including a confidentiality clause in the funding agreement.

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401 Supra 5, no. 12.
407 Supra 50, no. 126.
CHAPTER II. FULL DISCLOSURE OF THIRD-PARTY FUNDING AGREEMENTS?

228. If for any reason disclosure is required, only limited disclosure of TPF is tolerable.\textsuperscript{408} Naturally, the funder can agree to a full disclosure. In some situations this is beneficial for a funder, for instance where the claimant enters into settlement discussions and the disclosure of a funding agreement might bring additional pressure on the defendants to show that it has the financial wherewithal to pursue the claim.

229. Nevertheless, there are also funders in favour of a mandatory disclosure requirement and they are of the opinion that arbitral tribunals should automatically ask the parties to reveal both the funding relationship and the name of the funder in question.\textsuperscript{409} Among the proponents for disclosure, the majority is radically opposed to the systematic transmission of a full copy of the funding agreement, in contrast to the mere notification of the existence, as such, of the funding relationship.\textsuperscript{410} These funders thus do not want the entirety of the funding agreement to be disclosed because the agreement should not have any direct relationship to the arbitral tribunal’s decision. The author is under the impression that funders are not as adamant on this issue as it may appear. Hence, the author feels that that a disclosure obligation of the funding relationship, without disclosing the entire contents of the funding agreement, could be agreed upon if they would have adequate guarantees that the arbitral tribunal would not take the funding agreement into account in their decisions.

230. Why then are the funders so reluctant and even afraid for disclosure? NIEUWVELD gives a good example to explain the reasons for the scepticism towards a disclosure obligation. She gives the example of the defence insurance market in the USA. At times, an insurer’s presence is perceived as the presence of ‘deep pockets’ which could soften a jury’s discomfort in awarding large damages. Despite the absence of a jury in international arbitration, it is possible that a tribunal may feel more comfortable being less concerned about the damages when deeper pockets are involved. The tribunal may also – as described above\textsuperscript{411} – take the presence of a funder into account when deciding on security for costs or the allocation of the costs of the arbitration. NIEUWVELD concludes by saying that


\textsuperscript{411} Supra 73-80, nos. 194-212.
the question whether the ‘deep pocket’ phenomenon already exists in the TPF arena for international arbitration is premature to answer due to insufficient data at this time.412

231. In a response to NIEUWVELD’s blog, GOLDSMITH, SCHERER and FLECHET make an interesting remark regarding the reason not to disclose TPF due to the overriding fear that the claimant being funded might be perceived as backed by a ‘deep pocket’, which could give rise to potential counterclaims.413 They claim that in the absence of a liability insurance policy or some form of ATE liability insurance arrangement,414 the typical funder would not assume liability for the payment of damages resulting from the successful counterclaim. Furthermore, it would be very onerous to obtain such damages in international arbitration because the funder is a third party in the arbitral proceedings and third parties are generally not subject to the tribunal’s jurisdiction for purposes of awarding costs.415 Therefore, there would not be a reasonable basis for perceiving the funder as a ‘deep pocket’ for purposes of the claimant’s liability.

232. Another potential undesirable consequence of the disclosure of the funding agreement is the possibility that the arbitral tribunal will not award any costs to the prevailing claimant because the claimant did not incur any cost due to the funding of these costs by a funder.416

233. Finally, the opposing party might change its approach and its strategy when discovering the funding relationship. For instance, the opposing party could drag out the proceedings with the hopes of depleting the funder’s investment in the dispute.

234. It remains to be seen whether uniform standards will be established regarding a disclosure obligation for TPF agreements. The author expects that this issue will be dealt with in the near future. Nonetheless, it is worth discussing a proposal for a disclosure obligation while awaiting a binding solution from the arbitral institutions or the creators of ad hoc arbitration rules.

413 See the comment section at http://kluwerarbitrationblog.com/blog/2012/10/20/naiojong-oranje-hosts-third-party-funding-event/.
415 Supra 73-80, nos. 194-212.
416 For instance in Quasar de Valores SICAV S.A. and Others v. Russian Federation, SCC Case No. 079/2005, Final Award, 12 September 2010, the tribunal ruled that the claimant did not incur any costs because it received complete funding and was therefore not awarded any compensation for the costs it had sustained.
4. Proposal of a disclosure obligation

235. Due to the rise of TPF, arbitral institutions should adopt their rules to create a disclosure obligation of funding relationships, hence mitigating the risk for potential conflicts of interest. TRUSZ suggests an interesting proposal to the problems caused by TPF, which also addresses the concerns of funders against a disclosure obligation of the funding relationship.\footnote{TRUSZ, “Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration”, Geo. L. J. 2013, 1673-1674.} As explained above,\footnote{Supra 73-80, nos. 194-212.} one of the reasons why funders are reluctant to have the funding relationships disclosed and why they include confidentiality clauses in their funding agreements is that they fear that arbitrators will take it into consideration when deciding on the security for costs or the allocation of costs.

236. Another objection against disclosure was the concern that the opposing party could alter its strategy once he or she discovered the funding relationship.\footnote{Supra 86, no. 233.} TRUSZ tackles both these arguments with her proposal, by ensuring that the disclosed funding information will remain confidential if the funder and the claimholder choose to disclose their funding relationship and that the arbitral tribunal will not consider the relationship when deciding on awards of costs or security for costs. Put another way, the two main objections of funders against disclosure are covered and safeguarded in this proposal, thus incentivizing the funder and the claimholder to disclose their relationship and thereby preventing conflicts of interest. This also implies that the funder and the claimholder would have to release the confidentiality provisions of the contract. However, this would normally not be an issue anymore because the incentives to keep the relationship confidential are diminished by the proposal.

237. TRUSZ’s proposal consists of four different provisions and could be realistically achieved in practice because it requires only minimum changes to the current arbitral rules. Furthermore, this proposal also addresses the issue of who should bear the additional burden of identifying the funder and the possible conflicts of interest. The disclosure obligation can realistically be imposed on three entities: (i) the parties; or (ii) the arbitrators; or (iii) the arbitral institutions.\footnote{M. Scherer, A. Goldsmith and C. Fléchet, “Le financement par les tiers des procédures d’arbitrage international – une vue d’Europe Seconde partie: le débat juridique / Third Party Funding of International Arbitration Proceedings – A view from Europe Part II: The Legal Debate”, RDAI/IBLJ 2012, 653.} As the reader will notice hereafter, TRUSZ distributed the burden on all three, in lieu of the entire burden on one.
4.1. Arbitrator’s duty to disclose

238. First, the arbitrator has a duty to disclose any past and current relationships with funders to the institution.\footnote{J. TRUSZ, “Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration”, Geo. L. J. 2013, 1674-1675.} As mentioned above,\footnote{ Supra 66-68, nos. 171-179.} the arbitrators already have a disclosure obligation of information regarding conflicts of interest under the current institutional arbitration rules.\footnote{ This information has to be disclosed to respectively the ICC Secretariat (art. 11(2) ICC Arbitration Rules), the ICDR administrator (art. 7(1) ICDR Arbitration Rules), or the LCIA Registrar (art. 5.3. LCIA Arbitration Rules).} Considering that TPF relationships implicate independence concerns,\footnote{ Supra 63-66, nos. 162-170.} we can assume that, at least in theory, arbitrators have the obligation to disclose information concerning TPF. However, since arbitrators are most of the time not aware of the existence of TPF agreements and bearing in mind the unfamiliarity of many arbitrators with this recent phenomenon, they may deem it unnecessary to include such information in their disclosures. The arbitrators thus need the claimants and the funders to disclose the funding relationships and that’s where the next three provisions come into play.

4.2. Parties’ duty to disclose

239. Second, any party (i.e. both claimants and respondents) receiving outside funding must disclose to the institution this relationship. This disclosure shall include any potential conflicts of interest that may arise from other investments made by the funder.\footnote{J. TRUSZ, “Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration”, Geo. L. J. 2013, 1674-1675.} This provision requires the alteration of the arbitral rules because no such duty exists to date. In addition, funding agreements often contain confidentiality clauses,\footnote{ Supra 50, no. 126.} prohibiting parties to disclose the funding information. Due to the already confidential nature of arbitral proceedings, imposing a mandatory disclosure of the TPF relationship may not pose a problem to some funders because the opposing party would not learn of the funding relationship. However, this only covers one of the arguments of funders against a disclosure obligation, namely the fear that the adversary would change his or her strategy when discovering the funding relationship.

240. The other concern was that the arbitral tribunal might consider the TPF relationship when deciding on awards of costs or security for costs. A mandatory disclosure, absent any additional safeguards, will thus probably not convince many funders.
4.3. Conflicts of interest check by the arbitral institution

241. Third, in the event the funded party discloses potential conflicts of interest, the institution governing the arbitration will then automatically conduct a conflicts check. Additionally, the arbitral institution would have to keep all the funding information confidential.\textsuperscript{427} The arbitral institution would then, together with the information received from the arbitrators, have all the necessary information to complete the conflicts check. The arbitral institution would thus receive the information from the funded party and the arbitrators, rather than performing a due diligence itself.

242. At the Roundtable Discussions, imposing an active duty to investigate on the arbitral institution was vigorously opposed by practitioners because they believe that it is not the arbitral institutions’ task to solve the problems that are the responsibility of the other players in international arbitration (i.e. the parties and the arbitrators).\textsuperscript{428}

243. The concept of allowing the arbitral institution to initiate a conflict check is not new, as it is already provided in the ICC Arbitration Rules, where the ICC Secretary General is permitted to submit an arbitration challenge to the ICC Court if he or she is under the impression that the arbitrator in question should not be confirmed.\textsuperscript{429} If the arbitral institution would subsequently determine that there is in fact a conflict arising from a TPF relationship and that the arbitrator therefore has to be disqualified, the delicate issue of how to communicate their decision remains. The institution has two options: (i) it could acknowledge that the disqualification is due to a conflict of interest arising from a TPF relationship; and (ii) it could simply state that the arbitrator is disqualified due to a conflict of interest, without providing the reason. In the latter option, there is still the possibility that the parties assume that the disqualification was the result from a TPF relationship. This possibility of assumption, together with the overall need for some kind of transparency in the proceedings, makes the former option to most reasonable and feasible.\textsuperscript{430} The adversary would thus become aware of the funding relationship, something funders fear for several reasons.\textsuperscript{431} In light of these concerns, the former option would have to be accompanied by rules that determine to what extent arbitral tribunals may consider TPF relationships in their decisions on costs.\textsuperscript{432}

\textsuperscript{429} Art. 13(2) ICC Arbitration Rules.
\textsuperscript{431} Supra 85-86, no. 230.
\textsuperscript{432} Infra 90-91, nos. 245-247.
244. The author acknowledges that an automatic conflict check by the institution will be time-consuming and result in an increase of the already unduly expensive proceedings. However, in the event the non-independence of the arbitrator becomes known after the award is rendered and the award is subsequently annulled or denied recognition or enforcement, the costs will be dramatically higher than the costs resulting from the automatic conflict check because of the need to commence the entire arbitration anew.

4.4. Prohibition on taking third-party funding relationships into account by the arbitral tribunal

245. Finally, in order to prompt the voluntary disclosure of the funding relationship by the funder, it should be provided that the relationship cannot be considered by the arbitral tribunal for awards of costs or security for costs.\textsuperscript{433} One of the funders participating at the Roundtable Discussions shares this reasoning and states that arbitral institutions should be the frontrunner on this issue by amending their rules so as to impose a disclosure obligation for funding agreements. Such an obligation, according to this funder, should have to meet two preconditions: (i) the disclosure requirement applies to all parties involved;\textsuperscript{434} and (ii) there would have to be guarantees that the disclosure will not affect the arbitration proceedings.\textsuperscript{435} In essence, there must be some form of guarantee that the case will not be treated differently because a funder is involved.

246. This last provision implicates that the arbitral rules also have to be adapted on this issue because most rules give international arbitral tribunals significant discretion in determining awards for costs, save when the parties specified the allocation.\textsuperscript{436} Hence the fear among funders that the funding relationship may be taken into account by the arbitral tribunal in their decision on costs. As noted above, it is still highly debated whether the TPF agreement can be taken into account when considering awards of costs or security for costs.\textsuperscript{437} This proposal therefore expressly provides that the funding relationship cannot be considered by the tribunal and this would allegedly incentivize the voluntary disclosure because it gives a certain level of certainty to the parties of the funding agreement.\textsuperscript{438} However, it remains probable that the tribunal uses its discretion and states another reason for its decision than the TPF relationship, although it was in fact based on just that.

\textsuperscript{434} Supra 88, no. 238.
\textsuperscript{436} See e.g. art. 37 ICC Arbitration Rules; art. 31 ICDR Arbitration Rules; art. 28 LCIA Arbitration Rules.
\textsuperscript{437} Supra 73-80, nos. 194-212.
CHAPTER II. FULL DISCLOSURE OF THIRD-PARTY FUNDING AGREEMENTS?

247. The author is convinced that despite the erudite arguments in favour of considering funding relationships when deciding on the allocation of costs and security for costs, arbitral institutions should still adopt this proposal because the virtues of this rule, namely incentivizing funders to disclose the funding relationship and thereby preventing potential annulment or the denial of recognition and enforcement of the award, outweigh the possibility of claimants with insufficient financial recourses to abuse the arbitration proceedings.

4.5. Applicability to the UNCITRAL Arbitration Rules

248. Hitherto, the discussion has been on a proposal of a disclosure obligation of TPF relationships in institutional arbitration. The feasibility of such an obligation in ad hoc arbitration under the UNCITRAL Rules will now be considered. Due to the lack of a supervising institution in ad hoc arbitration, the different provisions of the proposal have to be modified in order to assure the same level of independence of the arbitrators in ad hoc arbitration as in institutional arbitration.\(^\text{440}\)

249. First, a party will disclose the TPF relationship to the appointing authority in lieu of to the supervising arbitral institution. The disclosure shall, just like the proposal for institutional arbitration, include conflicts that may arise from other investments made by the funder. Second, the appointing authority shall, upon receipt of notification from a party that it is receiving funding, request information from the arbitrators concerning the relationships with TPF corporations. This second provision is roughly the same as the first provision in the proposal for institutional arbitration. Third, the appointing authority, in lieu of the arbitral institution, shall conduct a conflicts check upon receipt of the arbitrators’ disclosures and the authority shall keep all information related to the TPF confidential. Finally, the arbitral tribunal shall – for the same reasons as in institutional arbitration – not be permitted to consider TPF relationships for awards of costs or security for costs.

250. The current UNCITRAL Rules permit parties to bring challenges of arbitrators to the appointing authority,\(^\text{441}\) specified in the arbitration agreement, or, absent such an agreement, the parties can request the Secretary-General of the Permanent Court of Arbitration (“PCA”) to specify the appointing authority.\(^\text{442}\) If the parties did specify an appointing authority, the funded party would have to disclose the funding relationship to this authority.

\(^{439}\) Supra 73-80, nos. 194-212.
\(^{441}\) Art. 13(4) UNCITRAL Rules.
\(^{442}\) Art. 6 UNCITRAL Rules.
251. Subsequently, the appointing authority should request information from the prospective or appointed arbitrators regarding the funding relationship and complete a conflicts of interest check once it has received the information. The appointing authority has to explicitly request this specific information because in *ad hoc* arbitration, prospective arbitrators do not disclose pertinent information to the appointing authority prior to their appointments. By doing so, the arbitrators will inevitably know that one of the parties is being funded since the appointing authority requested information related to their relationship with that funder. Hence, the reason why this proposal requires the arbitral tribunal to not consider TPF relationships in their decisions on awards of costs or security for costs, thus providing additional protection for the parties disclosing their TPF relationships.443

252. A problem could emerge if the parties did not specify an appointing authority in the agreement to arbitrate, and one of the parties requested the Secretary-General of the PCA to designate an appointing authority because the funded party is required, under this proposal, to disclose the TPF relationship to the appointing authority. By doing so, both the arbitrators and the opposing party will be implicitly informed of the funding relationship, considering that a conflicts of interest check by an appointing authority is only required when one of the parties is funded. Although the arbitral tribunal would still be prohibited from considering the TPF relationship for awards of costs or security for costs, the risks nevertheless remains that the opposing party will change his strategy once he or she receives this information.

253. Furthermore, requesting the Secretary-General of the PCA to appoint an appointing authority to perform a conflicts of interest check results in additional expenses, which can easily be avoided by simply informing the opposing party and the arbitrators of the fact that it is being funded, especially considering that the opposing party and arbitrators will implicitly find out about the funding relationship anyhow if the Secretary-General is requested to specify an appointing authority.444

254. It is the author’s view that the proposal for *ad hoc* arbitration by modifying the UNCITRAL Rules would not work as smoothly as the proposal for institutional arbitration. In the proposal for institutional arbitration, the arbitral institution will conduct an automatic conflicts of interest check, whereas in the proposal for *ad hoc* arbitration, the risk connected to disclosure of the TPF relationship is much larger because of the indications of a funding relationship for the opposing party. It should be noted that the parties could significantly allay the risk by selecting an appointing authority or, even better, by choosing for institutional arbitration, despite being more expensive, to resolve their dispute.

444 Ibid.
5. Conclusion

255. Both international commercial arbitration and the TPF industry – through confidentiality clauses – have a confidential nature. Although confidentiality is one of the main reasons why international commercial arbitration is such an attractive type of dispute resolution in international commerce, it nevertheless creates too many problems regarding the independence of arbitrators and the potential conflicts of interest to remain entirely confidential.

256. It is unquestionable that the industry of TPF in international commercial arbitration is growing stubbornly and steadily by leaps and bounds and will continue to grow in the future. However, the current arbitration rules are insufficiently equipped to address the problems of independence and disclosure in light of TPF relationships. Funders have a clear predilection for keeping their investment, as such, confidential. Hence, the initiative for a disclosure obligation rests with the arbitral institutions and the creators of ad hoc arbitration rules to take initiative and create a disclosure obligation for both the arbitrators and the funded parties.

257. By imposing the obligation on the arbitral institution to keep the disclosed information confidential and by prohibiting the arbitral tribunal to consider the TPF relationship in awards of costs and security for costs, the funders will likely be more willing to disclose the funding relationship. As a result, the parties will have more certainty regarding the sincerity of the arbitrator(s) independence. The author believes that such an obligation is necessary to safeguard the independence of the arbitrators and accompanying the strengths of international commercial arbitration as such.

258. However, to date, it is rather cumbersome to foresee whether funding agreements will be systematically subject to a disclosure obligation in international arbitration. Nevertheless, it is this author’s view that conflicts of interest and their potentially devastating consequences for arbitral awards and arbitral proceedings should foster reluctant funders and arbitral institutions in introducing a disclosure obligation.
CHAPTER III. REGULATION OF THE FUNDING INDUSTRY

1. General

259. Unlike lawyers, whose conduct is regulated by their local Bar or law society, funders are untethered from any overarching global or other regulatory regime. In brief, there is currently a virtual absence of any form of regulation for TPF in international arbitration, or as SEIDEL and SHERMAN put it, TPF is in an “embryonic regulatory state.”

260. However, the lack of regulation does not imply that TPF as such is or should be prohibited, or, put differently, that anything not expressly prohibited should be assumed to be permitted. The obvious reason for the lack of regulation is the newness of the TPF industry and there has not been an overriding appetite by the market and others for regulation. As the industry continues to grow, key jurisdictions (i.e. the U.K., Australia and the USA) are in the process of deciding whether to (further) regulate the industry. However, rules developed at a national level will not provide the solution for the issues on the level of international arbitration. It is the author’s view that the vital players in further regulation will be the arbitral institutions. These institutions are experienced pertaining to drafting arbitral rules and are thus in an ideal position to develop regulation, such as codes of conduct for arbitrators and attorney’s and disclosure obligations when TPF is involved.


447 Supra 18-20, no. 54.

261. Furthermore, arbitral tribunals generally do not have the powers to make orders against third parties due to the contractual nature of arbitration and this makes it even more intricate to regulate the conduct of funders.449

262. The question which subsequently arises is: should TPF be regulated or not, and if it is to be regulated, then by hard- or soft-law? Regulation is necessary to deal with some of the ethical issues; such as preventing the abusive success fees (e.g. 90% of the award proceeds),450 preventing excessive influence on the selection of arbitrators, and by doing so, defying the requirement of impartiality and independence; and preventing the unreasonable exploitation of attorney-client privilege.451 Regulation is also necessary to ensure that the funder has the financial capacity to see the case through, by imposing appropriate capital adequacy requirements.452

263. However, overzealous regulation risks curtailing the virtues associated with TPF because it could effectively hamper the access to arbitration453 for financially disadvantaged parties with meritorious claims.454 STEINITZ argues that the recent development and increase of TPF is due to a “de facto absence of professional regulations that enables funders and attorneys to operate outside of the disciplinary reach of bar associations.”455 Regulation could thus result in a reduced interest in TPF and accordingly exacerbate the access to justice.

264. The Code of Conduct for Litigation Funders (“Code”) issued by the Association of Litigation Funders of England and Wales (“ALF”)456 is an example of soft-law (i.e. non-binding) regulation,

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450 However, in Deloitte Touche Tohmatsu & Ors v. JP Morgan Portfolio Services Ltd. [2007] FCAFC 52, the Federal Court of Australia ruled that, despite the fact that the funder of the litigant controlled the proceedings completely and despite the funder taking the entire proceeds for itself, there was no abuse of process because the funder was the owner of the litigant; see for a discussion on this case.


453 Supra 25-27, nos. 67-72.


which will be discussed in-depth below. The reason for discussing a code of conduct for the funding of litigation is the simple fact that no such code is available yet for international arbitration. Nevertheless, this Code could prove to be the first – and highly praiseworthy – step in developing a code of conduct of TPF in arbitration. Furthermore, the possibility exists that international arbitration would be included in the Code in the future.

265. Working under this Code and learning from that experience is a good way to gradually become acquainted with it. It is probable that this Code is merely the first phase in a long process of regulatory developments. At some point, it may become necessary to replace the self-regulation by legislation if the voluntary regime would prove to be insufficient.

266. With the catastrophe of the sub-prime mortgages burned in the collective memory, the majority of the participants at the ICC Meeting felt that TPF needs to be regulated for the welfare of the arbitrating parties, for the protection of the reputation of funders and for the stability and the longevity of arbitration as an institution as such. MENON shares this opinion and rhetorically asks “if football were played without rules but with massive stakes and rewards, how would we condemn those playing the man instead of playing the ball?”

267. However, one must be careful not to stifle the industry through overly heavy regulation. With respect to international commercial and investment arbitration, CREMADES opines that soft-law solutions, like the Code, may be the only option reasonably available in the near future.

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www.judiciary.gov.uk/JCO%2FDocuments%2FCJC%2FPublications%2FCJC+papers%2FCode+of+Conduct+f or+Litigation+Funders+(November+2011).pdf; see also annex.

457 Infra 97-102, nos. 266-283.

458 The participants at the ICC Meeting considered the lack of regulation and control on behalf of the financial authorities as the origins of the collapse. B. CREMADES, “Concluding remarks” in B. CREMADES and A. DIMOLITSA (eds.), Dossier X: Third-party Funding in International Arbitration, Paris, ICC Publishing S.A., 2013, 154-155.


CHAPTER III. REGULATION OF THE FUNDING INDUSTRY

HARFOUCHE and SEARBY expect that voluntary codes of conduct will continue to be in effect until they prove to be ineffective – for instance because they lack enforceability – or if funders prove financially unstable. If this would prove to be the case, then statutory regulation will most likely follow. Finally, CRIVELLARO also believes that TPF should be regulated through soft-law instruments, which parties and arbitrators could then voluntarily adopt as binding in their respective cases.

2. Code of Conduct for funding of resolution of disputes within England and Wales

268. As said, there has been a first-ever attempt at voluntary self-regulation by third-party funders (i.e. the above-mentioned Code) in the U.K. Notwithstanding the fact that the Code is for litigation funders, it could also apply in arbitrations for funders, not only those based in England and Wales, but also to other funders when the seat of arbitration is situated in those jurisdictions. It is nonetheless regrettable that the international aspect is not covered at all in this Code.

269. This Code has been regarded and welcomed as a way to impose restraints on funding practices. For now, membership in the ALF and thus compliance with the Code is optional. Prima facie it seems that most funders join the ALF because clients are more reluctant to contract with funders that operate outside of the ALF. Although many have welcomed this Code, others have vilified it.

270. The following section will elaborate on the Code because this author considers it to be a good example of what TPF regulation could, and perhaps should look like.


465 Supra 95, no. 264.


467 Most of these restraints are deemed necessary because of the significant ethical concerns to which unregulated TPF could lead. See S. SEIDEL, “Maturing Nicely”, CDR May 2012, http://fulbrookmanagement.com/wp-content/uploads/2012/05/1May2012-Maturing-Nicelyb.pdf.


97
2.1. What is it?

271. The rather concise Code consists of ten principles that regulate the different stages of litigation funding agreements (“LFAs”), namely the formation, use and termination. LFAs are contractually binding between the funder and the client for the resolution of disputes within England and Wales. The wording “within England and Wales” give rise to some ambiguity because it is unsure if this wording solely refers to the location of the funder or the client or also to the seat of the dispute proceedings. This ambiguity may eventually result in non-U.K. funders joining the ALF in order to be able to offer funding to U.K. clients or foreign clients in arbitrations, which are seated in England or Wales.

272. The Code defines funder as someone who “has access to funds immediately within its control or acts as the exclusive investment advisor to an investment fund which has access to funds immediately within its control.” It is further stipulated that these funds must be sufficient to enable a litigant to meet the costs of resolving disputes by litigation or arbitration. Despite the fact the Code explicitly refers to litigants and litigants alone, it is also stated – which is rather ambiguous in the eyes of the author – that the Code can also be used in arbitration proceedings. Furthermore, funders are entitled to a share of the proceeds if the claim is successful, in return for the provided funding. Another restriction is imposed on funders because they are prohibited from seeking payment in excess of the proceeds of a successful claim, unless the litigant is in material breach of the LFA. The use of the wording ‘material breach’ is tenuous since it is not further defined in the Code.

273. The role of the funder and, more prominently, the limits of its role are also “loosely defined” in the Code. The funder must avoid taking steps “that cause or are likely to cause” the litigant’s lawyer to violate his professional duties. Furthermore, the funder must refrain from influencing that

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469 Only the most significant principles in the context of this thesis will be discussed.
470 Clause 6 Code.
472 Clause 2 Code.
473 Clause 2(a) Code. This provision articulates the non-recourse character, which is characteristic for TPF.
474 This provision resembles the restrictions imposed by the usury doctrine (supra 44-45, nos. 107-109).
475 Clause 2(b) Code.
attorney to cede control of the dispute.\textsuperscript{477} The Code thus expressly addresses the issue of conflicts of interest in the three-cornered relationship examined above.\textsuperscript{478}

274. In the Code it is also determined that funders need to maintain adequate financial resources. Unlike several other terms, the Code did define adequate financial resources. Adequate resources are enough resources to pay debts at all times and to cover aggregate funding liabilities under its LFAs for at least thirty-six months.\textsuperscript{479} \textit{Prima facie} it appears that this provision ensures sufficient cushion in case of financial difficulties.

275. Furthermore, the Code addresses the need to perform a due diligence\textsuperscript{480} by permitting the funder broad access to confidential information in order to assess the merits of the claim.\textsuperscript{481} It is also stated in the Code that the terms of the LFA shall control the extent of the funder’s ability to provide input on the litigant’s decisions in relation to settlement.\textsuperscript{482} As described above, having a properly negotiated funding agreement, which addresses issues such as the amount of input the funder can have during settlement negotiations, can prevent conflicts of interest in the so-called three-cornered relationship.\textsuperscript{483}

276. As for the termination of the LFAs, the Code requires that the LFAs state whether and how the funder can terminate the agreement.\textsuperscript{484} In the event the LFA grants a termination right to the funder, the Code limits that right to situations where the funder: (i) reasonably ceases to be satisfied with the merits of the dispute; (ii) reasonably believes that the dispute is no longer commercially viable; and (iii) reasonably believes the litigant is in material breach of the LFA. The Code curtails the funder’s discretion to terminate to these grounds.\textsuperscript{485} If the LFA granted the funder the right to terminate and the funder made use of this right, it will nevertheless remain liable for all funding obligations accrued to the date of termination, unless termination arises from the litigant’s material breach.\textsuperscript{486} As described above, some commentators feared that access to justice would be harmed if funders would terminate the funding agreement, for instance when they could be held liable for adverse costs awards. This provision counters that argument by forcing the funder to perform its funding obligations.\textsuperscript{487} As a final solution to the situation where a dispute about termination of the LFA cannot be settled, the Code

\textsuperscript{477} Clause 7(b and c) Code.
\textsuperscript{478} Supra 57-61, nos. 147-153.
\textsuperscript{479} Clause 7(d) Code.
\textsuperscript{480} Supra 36-37, nos. 87-90.
\textsuperscript{481} Clause 5 Code.
\textsuperscript{482} Clause 9(a) Code.
\textsuperscript{483} Supra 61-63, nos. 154-161.
\textsuperscript{484} Clause 9(b) Code.
\textsuperscript{485} Clause 10 Code.
\textsuperscript{486} Clause 11(a) Code.
\textsuperscript{487} Supra 78, no. 206.
foresees the right for both parties to obtain a binding opinion from a Queen’s Council.\footnote{Clause 11(b) Code.} The latter is in contrast with international arbitration funding agreements because it is customarily provided in these agreements that international arbitration will be used to resolve any disputes.\footnote{C. ROGERS, “Gamblers, Loan Sharks & Third-Party Funders” in C. ROGERS, Ethics in International Arbitration, Oxford University Press, forthcoming June 2014.}

277. Finally, funders must take reasonable steps to ensure that the litigant receives independent advice on the terms of the LFA. The Code stipulates that this requirement is met if it is confirmed in writing by the litigant that he or she has taken advice from the lawyer instructed in the underlying dispute.\footnote{Clause 7(a) Code.}

### 2.2. Criticism

278. The Code has been criticized for several reasons: (i) the lack of meaningful enforcement mechanisms; (ii) the fact that it is completely voluntarily and non-binding; (iii) its lack of detail; (iv) the possibility for potential conflicts of interest for counsel raised by funding; and (v) the lack of sufficient protection for potential defendants.\footnote{See U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, Comments on the Code of Conduct for Litigation Funders, 22 December 2011, 2 et seq. and www.instituteforlegalreform.com/uploads/sites/1/CJC_Code_of_Conduct_Comments.pdf; see also J. HYDE, “Code for litigation funding ‘toothless’, says critic”, L.S.Gaz. 12 December 2013, www.lawgazette.co.uk/law/code-for-litigation-funding-toothless-says-critic/5039182.article.} After examining the Code, the somewhat surprising conclusion of the ILR is that litigation funding should be discouraged in all circumstances and if it were permissible to occur at all, funding should be strictly regulated.\footnote{U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, Comments on the Code of Conduct for Litigation Funders, 22 December 2011, 9 and www.instituteforlegalreform.com/uploads/sites/1/CJC_Code_of_Conduct_Comments.pdf.}

279. The Code does not offer sufficient guarantees to avoid conflicts of interest that arise when legal counsel develops close relationships with funders. The Code only requires the funder to ensure that the litigant receives independent legal advice regarding the terms of an LFA.\footnote{Clause 7(a) Code.} As described above, some funders may exert influence on the choice of counsel and may have had previous relationships with the respective lawyer.\footnote{Supra 64-65, no. 167.} It is thus possible that such an outside legal advisor may have a financial interest in the funded claim.\footnote{U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, Comments on the Code of Conduct for Litigation Funders, 22 December 2011, 4 and www.instituteforlegalreform.com/uploads/sites/1/CJC_Code_of_Conduct_Comments.pdf.} For instance, imagine the situation where this outside advisor is simultaneously counsel to the litigant in the dispute in question. This is particularly problematic because the counsel is dependent on the claim being funded in order to earn legal fees.
Furthermore, the Code stipulates that the funders must not control litigation. The Code does not give further explanation on how to interpret control. Hence, the author’s view that referring to the word ‘control’, absent any specifications, is insufficient.

280. The ILR also notes that defendants are not addressed in the Code, hence lacking protection compared to the funded litigant. The respondents thus have little protection against frivolous or unsubstantiated claims, occasionally initiated, for instance to increase leverage for a settlement. This could also prompt the debate whether TPF is mainly focused on claimants and that TPF is a tool to attack defendants, regardless of the merits of the claim. This thesis has argued that TPF is available for defendants as well. In any event, provisions like these do not improve the atmosphere around TPF and this plays directly into the hands of critics, such as the ILR.

281. Furthermore, the ILR points out that a defendant seeking to recover an adverse costs award may be unable to do so, because the Code does not require funders to shoulder the litigants’ liability for cost awards. The Code only stipulates that the funder and the litigant can agree in the LFA that the funder will assume any liability of such costs. However, as described above, most funders are reluctant to bear such liability, since they already assume large financial risks. Hence, funders may refuse to shoulder the liability for payment of adverse cost awards, thus making a potential defendant vulnerable not only to being dragged into a frivolous claim, but also to being unable to recover its costs it would incur defending such a claim.

282. Finally, the Code contains no provision on the pressing issue of disclosure, hence leaving it to the parties to decide whether or not the funding should be disclosed. It is the author’s view that this omission is a clear indication of the ongoing disagreement within the funding community about disclosure and TPF in general.

496 Clause 7(c) Code.
498 Supra 27-29, nos. 73-76.
499 Supra 16, nos. 47-48.
501 Clause 8 Code.
502 Supra 77-78, no. 205.
2.3. Conclusion

283. The Code is undeniably a welcome first step towards regulation of an industry that heretofore was entirely unregulated. The attentive reader will have noticed that many of the issues that were identified and discussed throughout this thesis have been addressed in this Code and this has to be applauded. Nevertheless, many uncertainties and valid grounds of criticism remain. Moreover, the Code will only have a marginal, if any, impact on international arbitration due to the specificities and unique questions that arise in the arbitration context. It is however unquestionable that the international arbitration industry needs similar concerted efforts as the Code. Some of the rules from this Code could eventually be borrowed and modified when creating a code of conduct specifically for TPF in international arbitration.

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CONCLUDING REMARKS

“One thing is certain however: whether regulated or not, the use of third-party funding in major arbitration cases is a development that is here to stay.”

A. ENDICOTT, N. GIRALDO-CARRILLO and J. KALICKI

284. TPF in international commercial arbitration is a recent phenomenon, which is still in its infancy. The industry has experienced an awesome growth in media attention and scholarly work during the last couple of years. Notwithstanding this recent evolution, the industry remains a subject of some mystery. An illustrative example of this is the uncertainty surrounding the definition of TPF. The definitions range from every type of outside funding of a claim – which includes attorney financing, loans, legal expenses insurance, donations and assignments of claims – to the more narrow definitions, which this thesis baptized TPF sensu stricto. The latter is non-recourse financing of claims by a professional funder who has no interest in the case, other than a pecuniary one. However, despite the reported disagreement regarding the definition, it seems that most commentators wield the definition of TPF sensu stricto when addressing the notorious topic of TPF.

285. TPF is undeniably an exceptional method to outsource the financial risks connected with arbitral procedures. By providing this opportunity, financially distressed parties can vindicate their rights against larger companies, which increases the overall access to justice. Proponents of TPF unanimously stipulate the increase in access to justice as the key argument in favour of further development of TPF. Albeit the increase in access to justice and other advantages associated with TPF are lauded, some discernible adverse effects and problems can also be identified.

286. First, maintenance and related doctrines continue to pose problems for TPF in theory. These ancient common law doctrines were originally introduced to prevent the funding of claims by third parties. Prima facie these doctrines only apply in domestic litigation and not in international commercial arbitration. Nevertheless, this issue can play a role in international commercial arbitration, especially in the context of enforcement proceedings, which take place in domestic courts. However, through thorough investigation, it can be concluded that the effect of these doctrines has been relaxed in most jurisdictions to the extent where they are no longer an insurmountable obstacle for the validity of funding agreements. Nevertheless, the curtain has not yet fallen on this discussion and it is expected

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that this will be dealt with piecemeal in the domestic courts when the issue of the applicability of these doctrines to TPF agreements presents itself.

287. Second, the key issue of TPF at this stage of the debate is the fact that there is no disclosure obligation for funding agreements. This thesis has argued that arbitral institutions should develop such an obligation because the lack of transparency can cause several detrimental consequences. For instance, the confidential nature of TPF makes it extremely onerous to address potential conflicts of interest, both at the level of the so-called three-cornered relationship between the funder, funded party and the parties’ lawyer, and the level of the arbitrator(s). With respect to the three-cornered relationship, the presence of a funder could have the unwelcome consequence that the lawyer would favour the funder’s interest rather than the client’s interest, due to the power of the purse.

288. As for the conflicts of interest with respect to the arbitrators, the involvement of a funder could harm their independence and impartiality. The pressing need to maintain the impartiality and independence of arbitrators, which are generally considered to be fundamental principles of an arbitral procedure, may necessitate disclosure of TPF agreements. However, the funders have indicated on numerous occasions that they are reluctant to give up the common practice of keeping their funding relationships confidential. Their main fear is that arbitral tribunals will hold the funders liable for adverse costs awards and will order them to provide security for costs when the tribunal learns of the involvement of a funder. However, this thesis has argued that this fear is unfounded because the tribunal lacks jurisdictions in most cases to order the funder to pay such an award. The only legitimate concern of the funders is that the opposing party would alter its strategy once it becomes aware that its adversary is being funded. All things considered, the author deems it nevertheless necessary to impose such a disclosure obligation to safeguard the future of the international commercial arbitration industry as such.

289. Finally – this issue can be attributed to the newness of the industry – TPF is still virtually unregulated. The thoroughly discussed Code of Conduct by the Association of Litigation Funders has been – despite being criticised for reasons such as, its voluntary character and its lack of enforcement mechanisms – a welcome first step in what will most likely be an onerous journey towards the introduction of binding and profound regulation. This thesis has argued that some kind of regulation is deemed to be created and should be created in the future. However, more information is required about current practices, the nature of TPF, and the effects of TPF in international arbitration in order to be able to address the respective issues when developing meaningful regulation. While awaiting the arrival of hard data, it appears to be premature to draw clear-cut conclusions pertaining to this topic. If one decides to go forward with TPF, laws and regulations might help to avoid abuses or misuses of these new financing tools and this will ensure TPF from continuing to flourish. In any event, the aim
of this thesis was to consolidate the knowledge on this growing phenomenon in order to better and more efficiently deal with the issues and problems surrounding TPF.

290. After thorough examination and extensive research of this topic, the author concludes that TPF is currently somewhat of a proverbial ‘elephant in the room’ in the context of international commercial arbitration. Plenty of practitioners and commentators have heard of the existence, but are avoiding the confrontation to address the issues and the problems it may cause. The use of TPF and its peculiarities in the context of international commercial arbitration will undoubtedly become more clear in the near future when more case law is issued and common practices are developed. Hitherto, the majority of case law and statutes are focused on TPF in domestic litigation and international investment arbitration, which makes it nearly impossible at this stage of the debate to draw definitive conclusions about the status of TPF in international commercial arbitration. The lack of sufficient data seems to be the recurring theme in the story of TPF in international commercial arbitration and it appears that making educated guesses about the status of TPF in international commercial arbitration is what we are condemned to do until more data is available. Due to the need for transparency in investment arbitration, the author predicts that examining the use of TPF in international investment arbitration will continue to be the main source to turn to when light must be shed on the use of TPF in international commercial arbitration.

291. TPF is a fast growing industry and will unquestionably play a vital role in international commercial arbitration in the future by becoming a commonplace financing method for arbitral disputes. Whether in favour or radically opposed, TPF is, and will continue to be an important reality in the context of international commercial arbitration and further development should not be eschewed.

292. Finally, it should be noted that since TPF is such a cutting-edge industry, the likelihood exists that continuously debate and further development in practice will have provided several definitive answers to the questions identified in this thesis by the time this work is consulted by the reader.
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ANNEX – THE ASSOCIATION OF LITIGATION FUNDERS OF ENGLAND AND WALES: CODE OF CONDUCT FOR LITIGATION FUNDERS

1. This code (the Code) sets out standards of practice and behaviour to be observed by Funders who are Members of The Association of Litigation Funders of England & Wales.

2. A Funder has access to funds immediately within its control or acts as the exclusive investment advisor to an investment fund which has access to funds immediately within its control, such funds being invested pursuant to a Litigation Funding Agreement (LFA) to enable a Litigant to meet the costs of resolving disputes by litigation or arbitration (including pre-action costs) in return for the Funder:

   (a) receiving a share of the proceeds if the claim is successful (as defined in the LFA); and
   (b) not seeking any payment from the Litigant in excess of the amount of the proceeds of the dispute that is being funded, unless the Litigant is in material breach of the provisions of the LFA.

3. A Funder shall be deemed to have adopted the Code in respect of funding the resolution of disputes within England and Wales.

4. The promotional literature of a Funder must be clear and not misleading.

5. A Funder will observe the confidentiality of all information and documentation relating to the dispute to the extent that the law permits, and subject to the terms of any Confidentiality or Non-Disclosure Agreement agreed between the Funder and the Litigant.

6. A Litigation Funding Agreement is a contractually binding agreement entered into between a Funder and a Litigant relating to the resolution of disputes within England and Wales.

7. A Funder will:

   (a) take reasonable steps to ensure that the Litigant shall have received independent advice on the terms of the LFA, which obligation shall be satisfied if the Litigant confirms in writing to the Funder that the Litigant has taken advice from the solicitor instructed in the dispute;
   (b) not take any steps that cause or are likely to cause the Litigant’s solicitor or barrister to act in breach of their professional duties;
(c) not seek to influence the Litigant’s solicitor or barrister to cede control or conduct of the
dispute to the Funder;
(d) maintain at all times adequate financial resources to meet its obligations to fund all of the
disputes that it has agreed to fund, and in particular will maintain the capacity:
   (ii) to pay all debts when they become due and payable; and
   (ii) to cover aggregate funding liabilities under all of its LFAs for a minimum period of
36 months.

8. The LFA shall state whether (and if so to what extent) the Funder is liable to the Litigant to:
   (a) meet any liability for adverse costs;
   (b) pay any premium (including insurance premium tax) to obtain costs insurance;
   (c) provide security for costs;
   (d) meet any other financial liability.

9. The LFA shall state whether (and if so how) the Funder may:
   (a) provide input to the Litigant’s decisions in relation to settlements;
   (b) terminate the LFA in the event that the Funder:
       (iii) reasonably ceases to be satisfied about the merits of the dispute;
       (iii) reasonably believes that the dispute is no longer commercially viable; or
       (iii) reasonably believes that there has been a material breach of the LFA by the Litigant.

10. The LFA shall not establish a discretionary right for a Funder to terminate a LFA in the absence of
the circumstances described in clause 9(b).

11. If the LFA does give the Funder any of the rights described in clause 9 the LFA shall provide that:
   (a) if the Funder terminates the LFA, the Funder shall remain liable for all funding obligations
accrued to the date of termination unless the termination is due to a material breach under
clause 9(b)(iii);
   (b) if there is a dispute between the Funder and the Litigant about settlement or about termination
of the LFA, a binding opinion shall be obtained from a Queen’s Counsel who shall be
instructed jointly or nominated by the Chairman of the Bar Council.

This code is to be read in conjunction with the Articles and Rules of the Association of Litigation
Funders of England & Wales, which are available for inspection at:
‘Third-party funding’ (‘TPF’) – een financieringsmethode waarbij een entiteit die geen partij is in een arbitrageprocedure de juridische kosten van een andere partij draagt of een arbitrale uitspraak betaalt die uitgesproken werd tegen de betrokken partij, of beide - is momenteel een van de ‘hot topics’ in internationale handelsarbitrage. Het voorheen onbekende fenomeen is aan het evolueren naar een bloeiende praktijk en wint stelselmatig aan geloofwaardigheid in het collectieve bewustzijn van de juridische gemeenschap.

Een aanzienlijk aantal partijen onderzoeken nu de mogelijkheid om TPF te gebruiken om de noodzakelijke financiering te bekomen om hun vordering te bekostigen, in ruil voor een percentage van de toegekende compensatie indien de vordering slaagt. De financiering van de kosten die gepaard gaan met het nastreven van een vordering door een derde partij wordt stilaan onmisbaar voor onbemiddelde eisers om hun geschil te kunnen onderwerpen aan internationale handelsarbitrage.

Niettegenstaande de onbetwistbare voordelen die TPF met zich meebrengt, valt het evenzeer niet te ontkennen dat TPF ook een aantal gewichtige problemen kent. De voornaamste tekortkoming is het feit dat deze industrie virtueel ongereguleerd is en dat noch de gefinancierde partijen, noch de investeerders onderworpen zijn aan een verplichte mededelingsplicht met betrekking tot de financieringsovereenkomst, hetgeen tot verschillende, vaak ongewenste, gevolgen kan leiden.

Het eerste deel van de masterproef heeft als voornaamste doelstelling het schetsen van een kader voor TPF door het te bediscussiëren en analyseren van verschillende definities, alsook door het vergelijken van TPF met andere financieringsmechanismes. Vervolgens, na het beknopt bespreken van de geschiedenis van TPF, zal deze masterproef trachten de voornaamste redenen voor de recente groei van dit fenomeen te identificeren. Het tweede deel van deze masterproef zal gewijd worden aan het analyseren van de problemen die dienen te worden geadresseerd ten einde de groei van TPF te ondersteunen.

Deze masterproef zal zich voornamelijk concentreren op de toonaangevende jurisdicties met betrekking tot TPF; namelijk het Verenigd Koninkrijk, de Verenigde Staten van Amerika en Australië. De situatie in België zal in het kader van deze masterproef niet worden besproken, daar de praktijk van TPF hier nog niet noemenswaardig is ontwikkeld.