Kluwer Arbitration Blog

Can Third-Party Funding Find the Right Place in Investment Arbitration Rules?

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In early 2021, we wrote a post on this blog welcoming the inclusion of specific provisions on third-party funding (**TPF**) in the 2021 ICC Arbitration Rules. Recent regulatory developments in TPF in investor-State dispute settlement (**ISDS**), including publication of the VIAC Rules of Investment Arbitration and Mediation (**VIAC Investment Arbitration Rules**), have enticed us to revisit the subject.

TPF continues to move away from the dusty doctrines of champerty and maintenance (in common law) to becoming an established and recognized option for disputing parties. TPF is now a common tool in clients' and counsels' armory – increasingly for respondents (defense funding) as well as for claimants. According to Bloomberg Law's 2021 Litigation Finance Survey, most funders have increased their business despite the COVID-19 economic downturn, backed by growing interest and use by law firms and clients.

This expansion, amongst other things, has sparked institutions' and States' interest in regulating TPF. For practitioners, the changing landscape for TPF in institutional arbitration rules means that TPF should be considered not only when a dispute arises, but already when selecting and negotiating a suitable arbitration clause.

While some institutions have adopted a wait-and-see approach, others, e.g., ICC, CAM-CCBC, and HKIAC, have implemented provisions on TPF requiring disclosure of the existence of a TPF arrangement and the identity of the funder to assist in identification of any conflicts of interest. Of note is that these provisions do not require or allude to the disclosure of the funding agreement.

Another trend among arbitral institutions is to establish separate rules for commercial and investment arbitrations. For example, CIETAC, SCC, SIAC, and BAC have taken this approach. Most recently, VIAC has published the VIAC Rules of Investment Arbitration and Mediation. This is part of VIAC's efforts to promote the institution as an attractive option for administration of ISDS proceedings. As stated by VIAC's former Secretary General Alice Fremuth-Wolf, "*Vienna remains a commercial arbitration hub in Austria and Central and Eastern Europe. VIAC's new Investment Rules recognize calls by investors to fill a gap in the market, including the desire for a*

closer venue than the usual suspects of Washington D.C. and Paris. Adapting to investors' and States' expectations and needs, we look forward to seeing further growth of investment arbitration in this region". The VIAC Investment Arbitration Rules dedicate a specific provision to TPF (Article 13a).

VIAC's Investment Arbitration Rules were developed against the background of consideration of ISDS by other institutions, including ICSID (which just published Working Paper #6 on proposed revisions to its rules), UNCITRAL's Working Group III (which has received and published comments on its initial draft provisions on TPF (**WG III Initial Draft on TPF**) as part of its consideration of possible reform of ISDS), and the European Parliament (which has issued a report on Responsible Private Funding of Litigation).

Some of these institutions have considered going beyond requiring only disclosure of the existence of TPF and the identity of the funder. For instance, the current draft of ICSID's proposed revisions to its arbitration rules would explicitly allow tribunals to order the disclosure of "*further information regarding the funding agreement*". VIAC's new Investment Arbitration Rules have adopted this approach, providing that "*If it deems it necessary, the arbitral tribunal may order the disclosure of specific details of the third-party funding arrangement and/or the third-party funder's interest in the outcome of the proceedings, and/or whether or not the third-party funder has committed to undertake adverse costs liability.*"

Such provisions beg the question when, if ever, arbitral institutions or tribunals should require disclosure of information beyond the identity of the funder.

Disclosure of the Funder v. Disclosure of the Funding Agreement

The *raison d'être* of arbitral institutions and tribunals is to resolve disputes with a final and enforceable award. In this regard, the disclosure of the existence and identity of the funder can assist in assuring that no conflicts of interest taint the procedure or the award. Full or partial disclosure of the funding agreement is not needed to achieve this. On the contrary, disclosure of details of the funding agreement provides an unfair advantage to the non-funded party, creating an unbalanced position that arbitrators and arbitral institutions should avoid.

The ICSID Secretariat recognized in its Working Paper #5 on proposed revisions to the ICSID Arbitration Rules (at p. 279, paras. 42-43) that information regarding the funding agreement could be confidential business information, attorney-client privileged, or otherwise confidential and entitled to protection from disclosure.

Indeed, funding agreements are tailor-made to address specific financial needs of the funded party, containing commercially sensitive information about the funded party and the funder that is not relevant to the dispute. They reflect the funder's general policies, practices and pricing models as well as its view of the specific dispute that is being funded, including tactical assessments such as anticipated costs, procedural milestones, and duration of the proceeding. Having access to such information gives the opposing party inappropriate insight into the work product of the funded party's

counsel and an unfair advantage in the proceeding.

On the other hand, because funding agreements are the outcome of a mix of factors as well as negotiations between the funder and funded party, an opposing party or arbitrators may draw unwarranted conclusions from a funding agreement about the claimant's view of the merits of the case or its expected procedure or duration. The danger that a funding agreement will inappropriately impact an arbitrator's assessment of a case means that even *in camera* review of funding agreements should not be required absent compelling circumstances.

To date, ISDS tribunals have recognized the sensitive and irrelevant nature of funding arrangements. In *Oxus Gold plc v. Republic of Uzbekistan,* the tribunal determined that TPF had no impact on the proceedings and the terms of the funding agreement were irrelevant. The tribunal in *South America Silver v. Bolivia* ordered the claimant to disclose the funder's identity for the purpose of determining whether there was any potential conflict of interest, but denied disclosure of the funding agreement. In *Muhammet Çap v. Turkmenistan*, a rare case in which the arbitral tribunal ordered disclosure of the "*nature of the arrangements concluded with the third-party funder(s)*", French Courts ultimately refrained from compelling disclosure of the funding agreement.

The fact that the terms of a funding agreement are not relevant to disputes before arbitral tribunals is reflected in the revised arbitration rules of the ICC (Article 11(7)) and HKIAC (Article 44), which only require disclosure of the existence and identity of the funder. In the case of the ICC, the purpose is explicitly "*to assist prospective arbitrators and arbitrators in complying with*" their duties to disclose facts or circumstances that could give rise to doubts as to their independence or impartiality.

According to VIAC's former Secretary General Alice Fremuth-Wolf, the institution's goal in addressing TPF in the revised rules was primarily to ensure the independence and impartiality of the arbitrators. Disclosure of the existence and identity of the funder serves this purpose.

VIAC's Investment Arbitration Rules implicitly recognize that the terms of funding arrangements should rarely, if ever, be disclosed. Article 13a(3) does not require disclosure of funding agreements, referring instead to an arbitral tribunal's authority to order "*the disclosure of* ***specific details*** *of the third-party funding arrangement*" such as "*whether or not the third-party funder has committed to undertake adverse costs liability.*" Further, an arbitral tribunal should do so only "*[i]f it deems it* ***necessary***." (Article 13a(3), emphasis added).

An arbitral tribunal will rarely, if ever, be able to conclude that disclosure of details of a funding arrangement are "necessary". As we have written elsewhere, the fact that a party has entered into a funding arrangement is not sufficient to justify an order requiring the party to provide security for costs. Nor will the fact of a funding arrangement alone make it necessary – or even permissible – to inquire into the question whether the funder has committed to pay any adverse costs that may eventually be awarded.

What Does It Mean to Disclose the Existence and Identity of a Funder?

Article 6 of the VIAC Investment Arbitration Rules defines "third-party funding" as "*any agreement entered into with a natural or legal person* ***who is not a party to the proceedings or a party representative*** *(Article 13), to fund or provide any other material support to a party, directly or indirectly financing part or all of the costs of the proceedings either through a donation or a grant, or in exchange for remuneration or reimbursement that is wholly or partially dependent upon the outcome of the proceedings*" (emphasis added).

The ICC 2021 Arbitration Rules do not exclude party representatives: Article 11(7) requires disclosure of "*the existence and identity of* ***any non-party*** *which has entered into an arrangement for the funding of claims or defences and under which it has an economic interest in the outcome of the arbitration*" (emphasis added). Likewise, in Working Paper #5 (at pp. 277-278 and para. 41), the ICSID Secretariat accepted the suggestion that party representatives providing funding should not be excluded from the TPF disclosure requirement in proposed Rule 14. The HKIAC Arbitration Rules, in Articles 4.3(i), 5.1(g) and 44, require disclosure of the existence of any funding agreement and the identity of any third-party funder, without further defining these terms.

VIAC's exclusion of a party representative who may be financing the costs of the proceedings, for example an attorney working on a partial contingency basis, is consistent with the purpose of the inclusion of a provision on TPF in the VIAC rules: The identity of a party's representatives will be evident in the party's submissions, alerting potential arbitrators to facts or circumstances that may need to be disclosed in the VIAC Investment Arbitration Rules Article 16 arbitrator declaration.

The VIAC, ICC and HKIAC rules do not define what it means to disclose "*the identity*" of the third-party funder. But presumably the name of the funder should suffice: The potential for TPF to raise doubts about an arbitrator's impartiality or independence extends to circumstances such as where an arbitrator is a shareholder of a funder, sits on its investment committee, or has advised a funder during its due diligence in a case that is the same as or related to the arbitration that the arbitrator has been asked to determine. A potential arbitrator will know whether such circumstances exist as to any funder, such that the name of the funder that is supporting a party in a specific case would be sufficient to alert the potential arbitrator that they should decline the appointment or disclose the relevant circumstances.

On this topic, ICSID's Working Paper #6 has introduced a proposed revision to Arbitration Rule 14(1) that would require the parties to "*disclose the names of the persons and entities that own and control a funder that is a juridical person*". This is apparently in answer to the continued insistence of numerous States that parties be required to disclose the "*ultimate beneficial owner and corporate structure*" of any third-party funder, a proposal that the Secretariat had previously – appropriately – rejected (see WP #5, pp. 278-279, para. 39). For the reasons just stated, there is no need to provide such information to avoid inadvertent conflicts of interest or to allow

potential arbitrators to comply with their disclosure obligations. Furthermore, information about a fund's investors – particularly privately owned funds – is highly confidential and sensitive commercial information.

ICSID's proposed new revision would also require disclosure of more information about a third-party funder than is required of the party it is funding: Parties that are juridical persons currently are not required to disclose in the request to institute the arbitration the names of the persons or entities that own and control them. In Working Paper #5, the Secretariat rejected the proposal that ICSID Institution Rule 2(2)(d) be revised to make provision of information about the ownership and control of the party mandatory in the request. In its comments rejecting this addition, the Secretariat stated that the other party could request this information upon registration of the Request. At the same time, the Secretariat's comments insist that the purpose of requiring a **party** to disclose this information is to determine whether the dispute is **within the jurisdiction** of the Centre (see WP #5, p. 263, paras. 19-21). The Secretariat has again declined this proposal for the same reason in Working Paper #6 (at p. 16, para. 5). As a third-party funder is not the investor bringing the ICSID claim, the identity (in particular, the nationality) of the persons or entities that own and control the funder are of no relevance to the question of the Centre's jurisdiction.

The Future of TPF Regulation in Investment Arbitration

Much of the current debate surrounding regulation of TPF in investment arbitration is driven by misinformation about funding. In some cases, proposals for reform or revision of the rules are motivated by fundamental opposition to the availability of institutional arbitration to resolve investment treaty disputes.

In response to WG III's Initial Draft on TPF, the International Legal Finance Association (**ILFA**) submitted comments, including citation to extensive data, demonstrating that many of the concerns underlying the draft proposal were misplaced. ILFA has offered its assistance to the UNCITRAL Secretariat and WG III in their future deliberations. We also highlighted in our previous article the gatekeeping role funders have in filtering out unfounded and frivolous claims.

These points were echoed by the American Bar Association Section of International Law's comments on WG III's Initial Draft on TPF, which confirm that typically only ISDS claims with a high probability of success are able to obtain funding. The Section's comments also emphasized the important role that ISDS arbitration plays in holding States to the treaty obligations to which they have voluntarily consented, and that the availability of TPF in such cases supports access to justice and promotes the rule of law.

Policymakers should therefore see funders as friends, not foes. And institutions should consider whether proposals to regulate TPF in investment arbitration rules are based on sound information and a commitment to fair and balanced proceedings – or rather are driven by a desire to gain unfair advantage and to deter or prevent parties from seeking to enforce their rights.

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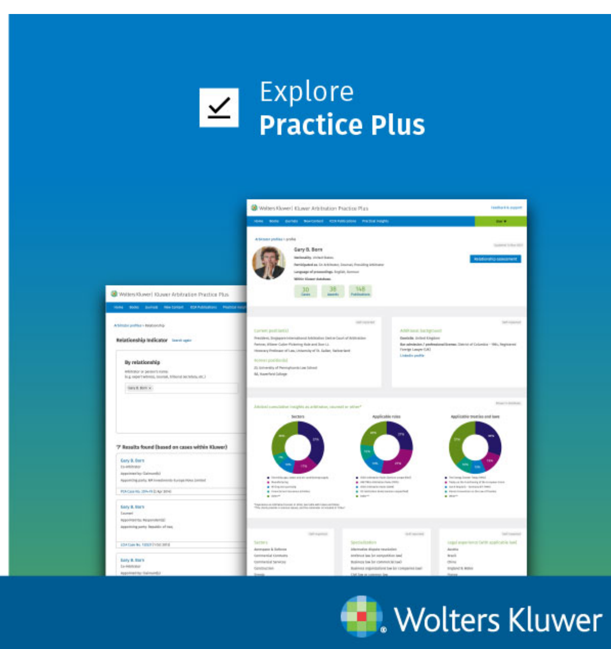

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