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Good governance of third party funding

by

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An OECD study shows that arbitration costs in investment disputes average US\$ 8 million; in one case involving mass claims, the parties spent almost US\$ 40 million in legal fees just to reach the decision on jurisdiction.¹ Under these circumstances, it is no wonder that third party funding has become the talk of the town.

Third party funding, *strictu sensu*, presents characteristics different from previously known forms of litigation funding (such as contingency fees or insurance): funders are often pure players; they invest in disputes for profit, although some may do it for a public interest purpose;² they are not necessarily attorneys themselves, although they employ attorneys to audit the disputes and evaluate the chances of winning the case;³ they often intervene at the outset of disputes and if cases go to arbitration, they sometimes participate directly in the nomination of the arbitral tribunal. However, they remain, legally speaking, third parties to the arbitration.⁴

Many call for regulation of this practice. I am of the opinion that regulation is not the way to go forward. Instead, arbitral institutions should adopt guidelines for arbitral tribunals.⁵

Regulation is unnecessary for many reasons.⁶ There are many different kinds of funders, and it is difficult to capture all forms taken by actors in the market in a single regulation. If there is to be regulation, it must not be at the national level but at the international level, particularly when funders intervene in international arbitrations. However, the likelihood of such international regulation being successfully negotiated in a reasonable period of time is close to zero. Even if one considers that such an international instrument might be adopted, it risks being outstripped by a fast moving practice and would soon be outdated. Governance administered by arbitration institutions would be the best tool to address third party funding.

Some of the best practices for arbitral tribunals confronted with third party financing could include the following:

- Financing by third parties must be disclosed for arbitration proceedings to be conducted appropriately.⁷ Whether financing contracts themselves must be disclosed is left to the tribunals' discretion.
- Depending on the extent of funders' control of the proceedings, tribunals may characterize funders as true parties.
- Funders should be obliged to follow the same confidentiality rules that apply to all parties in the arbitration.
- Funded parties must retain their own independent counsel.
- Funders must not cause, directly or indirectly, the funded parties' counsel to act in breach of their professional duties, nor take control of decisions to be made by counsel.
- Funders must not withdraw support during proceedings, unless under circumstances clearly provided for in the contract or if the funded party has acted in breach of the financing agreement.
- Tribunals may take into consideration third party financing when deciding on requests for security for costs.
- In decisions for cost allocation,⁸ tribunals may take into consideration the fees and costs incurred by funders if the relevant information was made available in the course of the proceedings. However, "investment premiums" should be financed out of the proceeds of awards and not be awarded in addition to the winning parties' compensation.

The ICC France Guide cited above was expected to take the lead in proposing these guidelines. Instead, it focused on the financing agreement only. A missed opportunity or a future challenge for ICC France?

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¹ OECD, "Government perspectives on investor-state dispute settlement: A progress report," Freedom of Investment Roundtable, December 14, 2012, <http://www.oecd.org/daf/inv/investment-policy/ISDSprogressreport.pdf>. Statistics for commercial arbitration are not as readily available, but cost is also a major concern for companies in commercial arbitration.

² Two investment cases are known to have been financed by charities: *Bernardus Henricus Funnekotter and others v. Republic of Zimbabwe*, ICSID ARB/05/6 and *Philip Morris Brand Sàrl and others v. Uruguay*, ICSID ARB/10/7.

³ 5 to 10% of the potential cases are said to be funded (ICC France Guide, *Le financement des arbitrages par des tiers financeurs*, §31). The guide was launched in May 2014 in Paris.

⁴ Even though some respondents have claimed that funders were the real claimant instead of the nominal claimant. See *Teinver S.A. and others v. The Argentine Republic*, ICSID ARB/09/1, *Rosinvest v. Russian Federation*, SCC Case No. 079/2005 and *Quasar de Valores SICAV S.A. and others v. The Russian Federation*, SCC Case No. 24/2007.

⁵ I am aware of the fact that this leaves out ad hoc arbitration, for which governance may have to be taken up by courts on a case-to-case basis.

⁶ By regulation, I mean a set of rules adopted by public authorities binding on funders. I do not consider self-regulation by funders as regulation, but a form of governance.

⁷ The involvement of funders bears directly on, *inter alia*, the admissibility of claims and a potential conflict of interest.

⁸ See *Kardassopoulos v. Georgia*, ICSID ARB/05/18.

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