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Coming out of the Closet: Third-Party Funding in International Arbitration

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The recent rise of third-party funding in international arbitration has opened a completely new dimension for arbitration itself. An opportunity of funding the parties of the process became a big deal breaker in many aspects that are visible at a first glance and those hidden behind the privacy clauses of funding agreements. This article is prepared in order to dive the readers into the changes of the procedural part: what circumstances change the vectors of development, who benefits from uncovering the financial facts, etc? The new figure comes into play and it is necessary to simulate possible variations of how it can influence the whole "game" of arbitration.

Introduction

Since 2012 the third-party funding (hereinafter – "TPF") market has grown rapidly by 500%, this figure corresponds to the increase of agreements and actual investors looking for particular cases.[1] Consequently, the topic of uncovering those who sponsor this market is currently on agenda of practitioners.

The urge that drives us to discuss such issue comes from the importance of such field for the business community in general. International commercial arbitration stays on the crossroads of law and trade while providing with solutions and benefits to both. It is important to improve this legal instrument and to keep it up to date so that the end consumers (private companies with impressive turnovers) are facilitated and satisfied. Even more, the world economy depends on arbitration, the GDP of every country directly depends on how the businesses make the deals and, in case it is necessary, solve possible disagreements with the help of arbitration. With this being said, we cannot undermine the importance of a single aspect of international commercial arbitration, especially the third-party funding.

The mentioned above issue starts to be addressed more often by the European research academia and international community on various levels. Notwithstanding, it is necessary to mention following: scientific majority, in most of the cases, while observing such aspect, highlights the issue irregardless of the physical borders since international commercial arbitration presumes no borders in its essence. It is an autonomous field with

its own fundamental regulatory acts (New York Convention 1958)[2] but yet very customizable and rather free from local obligations. This article will highlight the progress on different levels (countries, supranational organisations etc) but purely for informative reasons in order to underline the progress that has been done around the globe.

The research is based on the recent academic publications and statistical data from the circle of European and international academics (David Abrahams, Derric Yeoh, Edouard Bertrand, Jeniffer Trusz, Jern-Fei Ng etc.) solely on the matters of the third-party funding. For those readers, who are not fully accustomed with the basics of the international arbitration, the author recommends to refer an attention towards the books of Gaillard Emmanuel[3], Margaret Moses[4] and others. Alongside the work, particular scientific methods were used so to achieve the best result possible, among them: comparison method, historical method, statistical method, model method etc.

While drafting the practical part, the briefings of the private companies, particular cases and recent professional opinions were utilised in order to provide the readers with the insights coming from the real business world (e.g. roundtable discussions of private companies). However, elaborating on the practical part still appears as a challenge due to a high level of privacy.

1. **The battle of transparency against the privacy**

When entering into the TPF, the funder is rather not interested to be revealed due to a simple reason of confidentiality in the business world[5]. It is fair to say that the same reason was one of the triggers for creating the arbitration in general – so to avoid extra eyes glancing the disputes.

However, nowadays trend prioritises the transparency over confidentiality in the matters of international arbitration. In the Queen Mary International Arbitration Survey 2015[6] many practitioners expressed strong desire in the need of TPF being disclosed. However, the most peculiar aspect was that soft law was chosen as the way of how to implement such desire. The business, as usual, wants it to be less radical. Nevertheless, many national legislators have gone further and decided not to limit themselves only with the soft law but to envisage a mandatory clause obligating the parties to disclose the TPF in arbitration relations.

It seems rather clear that this aspect starts to be addressed more often on all the levels: (a) National, (b) Regional and (c) Institutional. In author's opinion, such differentiation represents the best overall picture by going one layer after another with providing the notorious examples on each level.

(a) National level

Australia is considered as a forerunner in funding the arbitration by third parties. It is a big industry that was first limited to bankruptcy cases but subsequently expanded on civil matters of all kinds. One of the major cases that helped the TPF to spread and gain its power was *Campbells Cash & Carry Party, Ltd. v Fostif Party Ltd.*[7] that provided the funder with a wide range of control over the case itself.

The Australian High Court confirmed that funding agreement was not in abuse of local laws. Thus, the claim of the opponent based on such ground was dismissed. The panel justified the presence of the funders and the influence over the case in various matters: appointment of own legal team, deciding on the crucial aspects concerning settlements, variations in choosing the defence tactics etc. Such case, accordingly, triggered the changes on the legislative level based on the argument of support of consumer rights.

The High Court of Australia added that any risk of over influencing the case should be precluded by the professional code of conduct, which always stands, regardless of the legislation gaps concerning the TPF. Such rules oblige the advocates to perform on behalf and in the best interest of the client.[8]

Recent legislative update coming from Singapore prescribes the requirements necessary for the TPF being revealed to the parties. It became obligatory to disclose the fact of funding together with the identity of the funder.[9] Nevertheless, the terms of the agreement may still be kept confidential.

Furthermore, there are some sanctions expected to appear when the funder constitutes non-compliance with the funding agreement in Singapore. This is done so to avoid any bias happening during the arbitration process when the other party may expect the opponent to have the financial support but be mistaken by that.

The reason for such updates lies behind the aspirations of Singapore to strengthen its position at the arbitration market in Asia[10] and to keep up with the modern trend of sponsoring arbitration, which has been already utilised by other well-known arbitration arenas (London, Hong Kong, Vienna etc).[11]

(b) Regional level

The update concerning the disclosure of TPF also came from the European Union, which is currently seeking the conclusion of FTA agreement with Vietnam and other international partners[12]. The clauses requiring the TPF to be disclosed in the arbitration proceedings have been envisaged into the mentioned above FTA agreements. Such clause prescribes to notify the tribunal of arbitrators about the fact of TPF, nature of the agreement itself and the contact details of the funder (full name, address). No other details are required.[13]

The same applies for the EU-Canada relations – the update on the free trade agreement was carried out by the partners and constituted into the Comprehensive Economic and Trade Agreement (hereinafter – CETA)[14]. While resolving the disputes in a specially created tribunals, CETA obliges third-party funders to be immediately uncovered.[15] Even more, the fact of sponsorship may be taken into account by the tribunal while deciding on allocating the security costs. The usage of such controversial method does not receive much of appreciation from the side of the author. The funders are not amused of the possibility to be engaged as a party of the process since this might oblige to pay more than the funding contract prescribes.

Nevertheless, such a tribunal is an *ad hoc* being exclusively created for the purposes of resolving disputes arising from the trade relations between the partners and should not be influencing the trade relations outside of its scope nor be a precedent for other cases.

(c) Institutional level[16]

The first attempts to regulate the TPF by the arbitration institution were carried out by the Association of Litigation Funders of England and Wales. Such organisation came up with the first in kind Code of Conduct for the mentioned above industry.[17] Later one the practitioners commented[18] that such Code was rather vague leaving big blanks in most important areas without being actually binding for those, arbitrating outside the institution.[19] However, the problem of obligation to follow the rules in particular jurisdiction will always stand due to shortcomings of international law. The positive influence that brings such endeavours rests in attempts rather than actual results.

The Singapore International Arbitration Centre has also released new arbitration rules that fit purely for investment arbitration. Such rules provide with explicit power for arbitrators to order the disclosure of TPF while deciding on the particular case.[20]

Additional aspect that should be touched when commenting about the institutional level is an authority of such institutions in creating the lists of trustworthy funders along with the already known lists of arbitrators. The academicians[21] elaborate on this issue as an important aspect of the overall regulation of TPF worldwide. This step may also bring in line all the requirements necessary for the funders to be achieved in order to sponsor the party of the process. It seems quite complicated for the author to imagine unified standards of compliancy for the funders across the world. However, it is a good trend towards regulating the field. To add to this, it is better to have different requirements at different institutions than to have none at all.

2. **The Client-Funder-Lawyer triangle**

When the funder swirls into the arbitration, it breaks the standard lineal Client – Lawyer relationships by creating a triangle of Client – Funder – Lawyer relationships. Moreover, the funder himself stands on top of them. Depending on the funding agreement, the sponsor may exercise almost full control over the case, the so called “hands on” approach (deciding the arbitrators panel, lawyer, position of the party and forming the position up until the final order or deal with another party) or take it easy and observe the situation from the side (“hands off” approach).[22] Considering the fact that every investor cares about the income he will receive from the money invested, it is reasonable to think that most of the funders might want to influence the case at least at some manner and engage into the process their own legal team.

Edouard Bertrand, in his book underlined that the funder, in a strictly legal sense, is not a party to arbitration since one does not receive any rights or obligations. However, in an economical sense, the funder is a party due to a reason that if the opponent raises a strong defence, it will influence the defendant and the funder in a direct manner.[23] Thus, even not present at the hearings physically, he receives the same legal “punch” as a defendant.

Due to that, the funder is ought to influence both the client and the lawyer in case he wants to recover his money. The right to decide partially passes to the one who sponsors the whole process. When the client might want to agree on the deal with another party without going further, the funder might not be willing to agree with this and will try to push it forward just because such deal will not bring expected profits. Meanwhile, the lawyer, who *de jure* owes the duty to the client, *de facto* shifts such duty to the funder.

This turns out in giving such advices to the client that are not necessarily in his best interest simply because the funder has decided on particular lawyer and he is his paymaster.

This triggers the ethical question that might stand on the path of the future of the TPF. However, we might argue in defence that the TPF agreement, as any other private contract, can be terminated by the request of one of the parties. Even though it seems that the funder is on a top of a "TPF triangle", the client can go beyond that and simply break the deal by refusing the interference of the funder. However, this seems rather illogical since the main idea of TPF is to receive the money for the purpose of arbitration. Thus, both, the client and the funder have one common aim – to win the case and to recover the damages meaning that they are well aware about the rules of the game and are willing to play it. Even more, neither client nor funder will go for such extremes since they both act in a reasonable way with pursuing the same interest.

3. **Modes of disclosure**

While discussing the institutions and countries being concerned by such issue, it is worth mentioning the types of disclosure used in arbitration process. We will explore such phenomena based on distinctive feature of the amount of information that is revealed about the TPF:

(a) Full disclosure

It is a very rare case when full disclosure may occur. The principle it is based on, is giving the full information about the funder, the funding agreement and other details including price, the interest rate etc. Such approach may infringe the sanctity of the private contracts and fundamental principles of civil law. The only justification for full disclosure may be reasoned by the need of affirming the fact that arbitrator is independent while deciding particular case. It might be invoked when there is a negative and possible likelihood for the arbitration process to be terminated in the middle, or even worse – at the final stage due to dependency of the arbitrator.[24]

Nevertheless, it is possible to avoid such an extreme measure with the improvement of arbitration rules, especially on the institutional level. Jeniffer Trusz in the article *"Full Disclosure? Conflicts of Interest rising from Thid-Party Funding in International Arbitration"* proposed simple but yet extremely useful solution.[25] The professor offers a four-step system of rules that should be incorporated by the arbitration institutions for the mechanism of disclosure of TPF without the need of going into full disclosure.

(b) Partial disclosure

This form of disclosure respects the sanctity and privacy of the agreement concluded between the funder and the funded party. It requires disclosing the mere fact of the funding without going into details and informing about the terms of the agreement. One of the issues that may arise in this case is that the TPF may be nominal, meaning that the opponent may not know for what exact amount the party was funded (it can be full funding or partial). On the other side, the influence that it brings for the case may exceed

any expectations in a positive manner – another party may be willing to settle the dispute without even having the knowledge about the minimum funding level.

Notwithstanding, what if the price of the funding agreement is $1 USD? The opponent and the panel will not be aware about such details since, usually, they are not revealed – only the mere fact of sponsorship is communicated to the parties of the process. Thus, the opponent may make an offer based on the knowledge that the other party is sponsored without realising that the amount of investments equals to almost nothing. This creates a negative influence on the arbitration process leaving the opponent being not well informed and because of that, the opponent might be forced to make an offer which he would not make otherwise. This issue is something fresh on the "TPF market" since it has not been discussed yet.[26] In order to eliminate this gap, the arbitration institutions might consider including the obligation to reveal the price while drafting the update of rules.

For better or for worse, TPF has conquered most major arbitration arenas leaving the practitioners and academics with the urge of proposing the way how such mechanism may be smoothly implemented into the whole architecture of arbitration.

4. The changes: positive-negative ratio

If we consider the benefits of disclosure, many positive aspects may be mentioned. One of the most important – elimination of the possible conflict of interest between the revealed funder and other parties of the process, support of justice by providing the weaker party with an opportunity for defence, rise of economy by boosting the investment industry and, the last but not least, changing the negative approach towards the mechanism of TPF.

Australian experience shows the following: it is confirmed statistically that the cases being funded by the TPF are less likely to be reversed and are more citied in the scientific researches. The reason behind that is the funder himself, who assesses the case thoroughly with selecting the lawsuits that have prediction of winning at least of 70%.[27] It may sound as an exaggeration, but the TPF will be a story of success because it deals with successful cases in the matters of the trustful parties, reliable panel of arbitrators etc. Thus, there is no reason for the funder to hide in the shade. The presence of the investments should be considered as an indication of quality mark.

These day, it is no longer a problem to get the side funding which was previously called *maintenance* or *champerty* in common law practise and was prohibited by most of the States.[28] Such definition traces back to the medieval ages aiming against fraudulent practices of high figures intermeddling into the court procedures.[29] The justification against that was straightforward: no gambling should be done when the justice is dispensed

Thus, no medieval practices are applied any more. There are many instruments available in order to indicate the fraud rather than prohibiting the whole industry based on the "once and for all" principle. Both parties of the process are free to get the funding; the only matter is to check whether it does not influence the arbitration process in a negative manner. A good way to ensure this is to come up with an update of institutional rules, which is already on its way. Even more, the author suggests to consider the opportunity

of creating the new treaty – the New York Convention II [30]aimed to facilitate this sphere and other potential fields lacking the uniformity in regulation. Such proposal will become a new chapter and logical continuation of the original Convention. Additionally, it as a chance to power up the positive influence over the arbitration industry while sticking to the uniformity principle.

The pro argument of proposing the New York Convention II is the interest of the states to become signatories due to purely economic reason. It may sound harsh, however it is a proven fact that majority, if not all signatory states follow the New York Convention 1958 impeccably. Even such a big player at the international arena as Russia, which at times is not willing to implement he decisions of the European Court of Human Rights[31], strictly follows the New York Convention 1958 on the matters of arbitration. The reason for that is simple – the money matter makes its influence. It is in the best interests of every state to create good conditions for arbitration in order to gain from that. Unlike, for example, the Convention on Human Rights[32] which brings to the State nothing but the economic loss.[33]

The same mechanism of "money reason" was put before and should be inserted into the fundaments of the new international treaty again. This will unify the rules on third-party funding in international commercial arbitration, and provide with the useful method of regulating the TPF industry.

What are the negative sides? While deciding, the arbitrator may put an obligation to cover the security costs by the funder, despite the mentioned already fact, that the funder is not a party of the process in a strictly legal sense. This pushes the investors to go behind the "curtain" of privacy clauses, again. Such fears have been offset by the recent cases. In *Kardassopoulos v. Georgia* case of 2010, it was confirmed by the arbitrators that the funder should cover no security costs[34]. However, it is quite complicated to change the overall attitude of the funders[35] just by a handful of cases. What needs to be addressed in here is the solid assurance of preventive clauses being put into arbitration rules of particular institutions confirming such approach.

The academician Derric Yeoh expresses an idea that TPF can become a slippery slope for the arbitration process due to many factors that have been mentioned already. However, it is not only the TPF that can do so, there are many potential risks arising every day in different legal fields, and not only the legal ones. Thus, much wiser move would be not to prohibit the TPF in particular parts but to create an instrument that regulates it.[36]

Meanwhile, it is obvious that positive aspects outweigh the negative ones without any doubts. Yet, the main approach in international arbitration concerning TPF was in applying the policy "Don't ask, Don't tell" which evidently has seen better days. This article became an opportunity to underline phenomena of third-party funding and guide the readers through the new path of more transparent arbitration process. The approach that is transparent not towards the public, but exclusively towards the parties of the process, meaning, that arbitration itself does not lose its major benefit – the privacy. It is fair to say that both parties including the arbitrators' panel deserve to know who are the players behind the curtains, and whether they exist in general.

Overall, the main message that needs to be addressed as a closing line: TPF comes out of the closet. Third-party funding becomes public not in harm to the parties but for the benefits of the process.

Conclusions

Following the thorough research of the topic and applying various approaches so to receive the best result possible, following conclusions may be provided:

1. The TPF is a recent trend in arbitration that becomes popular with astronomic progression. The statistical data shows the rise of interest among investors for more than 500%. This triggers the developing of new field of arbitration that is, however, lacks some primary regulation and universal approach.
2. The countries, which are known as being world arenas for the international arbitration have already adopted the regulations concerning the TPF. This is a signal of importance of TPF and the call to the world governments to do the same.
3. It is not only countries who update their laws, such changes have also reached out the regional and supranational organisations especially in the field of trade, for example, the trade agreements that have been highlighted (EU-Canada, EU-Vietnam) in this article give a clear understanding of importance of TPF on all the levels.
4. International arbitration institutions that are relatively autonomous make their own effort towards updating the rules so to assist the TPF and to make it more efficient. Such institutions might become the locomotives, influencing the creation of more unified legislation for TPF.
5. The changes of classical lineal relations "client-lawyer" in procedural part of arbitration were discussed. The entrance of the new figure into play – the funder, changes the weight system and shifts the lawyer's duty to the person who sponsors him. Eventually this heavily influences the decisions of the party of the process who is behaving under the money influence from the funder.
6. Additional attention was given to procedural aspect in the case where the party of the process is nominally funded so just to be called funded (e.g. the fact of the funding is existent, however the party receives only 1 US dollar). When the party receives the title of being funded, it changes the approach the opponent will take, without even realising that the funding agreement is nominal.
7. The proposal of drafting the new international Treaty aimed towards regulating the TPF in international arbitration by example of the New York Convention 1958 was communicated. The author proposed simple but yet efficient method of assuring the implementation of such Treaty by the governments.
8. Overall message that was distilled from the article comes as follows: "The changes make no harm to the essential value of arbitration – its privacy – but rather serve as an extra instrument in supporting the justice, if the process of sponsorship is done according to the commonly accepted standards."

Footnotes

[1] DELANEY, J. Mistakes to avoid while approaching third-party funders. Global Arbitration Review, 2014, p..9.

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[6] See official web-site http://www.arbitration.qmul.ac.uk/research/2015/ [last accessed 8 May 2017].

[7] Campbells Cash & Carry Party, Ltd. v Fostif Party Ltd (2006) 229 ALR 58 (Australia).

[8] Singapore Legal Profession (Professional Conduct) Rules, r. 2(2)(c).

[9] See official web site of the Parliament of Singapore https://www.parliament.gov.sg/sites/default/files/Civil%20Law%20%28Amendment%29%20Bill%2038-2016.pdf [last accessed 21 May.2017].

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[13] EU-Vietnam Free Trade Agreement Article 11, p. 33. See the electronic copy: http://trade.ec.europa.eu/doclib/docs/2016/february/tradoc_154210.pdf

[14] Comprehensive Economic and Trade Agreement between EU and Canada. See the text on the official web site http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf [last accessed 07 June 2017].

[15] Dechert's Law Firm, Theh EU succeeds in establishing a permanent investment court in its trade treaties with Canada and Vietnam, Legal briefing from the Dechert's International Arbitration, 2016.

[16] Author's commentary: by the institutional level the author implies to the international arbitration institutions that are established by private entities or governments

and provide their own rules (e.g. the Arbitration Institute of the Stockholm Chamber of Commerce etc). The research would not be full without mentioning such institutions.

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[20] SIAC Investment Arbitration Rules 2017; and the official web-site http://www.siac.org.sg [last accessed 05 May 2017]

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[23] BERTRAND, E. The Brave New World of Arbitration: Third-Party Funding, ASA Bulletin, 2011 p.610.

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[25] TRUSZ, J. Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Arbitration, 2013, p.1661-1673.

[26] Such comment is made based on the best knowledge of the author/

[27] ABRAHAMAS, D. & CHIEN. D, A Market of Justice: A First Empirical Look at The Third Party Litigation Funding, 15(4) J.Bus. L. 1075, 2014, p.1105-1106.

[28] REDERN, A. & HUNTER, M. International Commercial Arbitration, Thomson Sweet & Maxwell 2004, p.10-17

[29] JERN-FEI, N. The Roles of the Doctrines of Champerty and Maintenance in Arbitration, Essex Court Chambers, 2010.

[30] In this matter the author refers to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 as a great example of unified regulation of international commercial arbitration across the world.

[31] News article: Russian Federation: Constitutional Court Allows Country to Ignore ECHR Rulings, Library of Congress 18.05.2016 see the official web site http://www.loc.gov/law/foreign-news/article/russian-federation-constitutional-court-allows-country-to-ignore-echr-rulings/ [last accessed 09 June 2017].

[32] The Convention for the Protection of Human Rights and Fundamental Freedoms, 4.11.1950, Rome.

[33] Author's commentary: by highlighting this aspect, the author does not, in any matter, tries to undermine the importance of the European Court of Human Rights or deprive the importance of fundamental rights. This comment rather serves as a message to the society on nowadays disbalance in various rights and how different the approaches of governments to different corpus of rights. The same situation is applied not only to the Russian Federation but also to Ukraine and other European States.

[34] Kardassapoulos case, ICISD Case Nos. ARB/05/18, ARB/07/15.

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