Financial support

Alex Hickson and **Adam Erusalimsky** on funding for international arbitration

Arbitration provides an alternative to litigation pursued through jurisdictional courts, which offers flexibility and control to the parties involved in a dispute. But it is often costly, due to the complex commercial nature of the dispute – particularly where it involves transnational parties and raises issues of conflicts of laws – and the sophisticated, specialist counsel at premier law firms engaged by the parties to assist in its resolution.

In a 2018 survey produced by law firm White & Case in partnership with the School of International Arbitration, 67% of survey respondents, which included private practitioners, full-time arbitrators, in-house counsel, experts and other stakeholders, indicated that the cost of the process was the worst feature of international arbitration. While the cost of international arbitration most likely reflects the complex, commercial and often cross-border nature of the disputes being arbitrated, rather than any inefficiency of arbitration procedures or the parties involved, it can be burdensome on claimants. Increasingly, third-party funding is sought to ease the pressure of these burdens.

Third-party funding allows impecunious claimants to pursue meritorious claims, who ordinarily might not have the resources to seek the redress they are entitled to. It can also be used to allow well-resourced claimants to hedge their legal costs risk and reduce the burden of legal costs on their balance sheet.

FUNDING BENEFITS

In a typical funding arrangement, the third-party funder shoulders most of the risk. The advantages of arbitration funding for both lawyer and claimant are substantial. Most fundamentally, third-party funding facilitates access to justice. A capital-constrained claimant who might not otherwise have the resources to prosecute its claim (sometimes as a direct result of the defendant's wrongful conduct) is given the opportunity to have its day in court. This is particularly true in 'David v Goliath' cases where a smaller claimant takes on a bigger, better-resourced defendant, who may use a strategy of attrition to exhaust the claimant's appetite and ability to prosecute its claim. Partnering with a well-capitalised funder substantially levels the playing field and allows a claim to proceed on its merits, rather than on the respective parties' purchasing power.

Even where a claimant has the resources to fund a dispute, funding offers many advantages. Third-party funding allows a claimant to unlock the value of a potential claim and preserve capital for other uses, while transferring the ongoing costs and contingent liabilities of the claim to the funder. Moreover, funding can take the potentially significant expense of arbitration off a company's books. Ultimately, funding permits a claimant to hedge its risk, ensuring that it will be in a better position if the claim is successful, but in no worse position if the claim is not successful. So funding transforms litigation from a traditional 'win-lose' proposition to a 'win-don't lose' proposition.

In some instances, the costs associated with arbitration funding incurred by a funded party in an arbitration might be recoverable from the other party to the arbitration. In the landmark case of *Essar v Norscot* [2016] EWHC 2361 (Comm), the tribunal found that Essar's conduct had effectively caused Norscot's impecuniosity and forced it to seek third-party funding from Woodsford. Therefore, the tribunal held that it was right and proper that Essar should pay Norscot's funding costs, including the success fee that had become payable to us. The tribunal found that because Essar had deliberately put Norscot in a position where it could not fund the arbitration on its own, it was reasonable for it to obtain funding from Woodsford on the terms that it did. Additionally, such funding costs were 'other costs' for the purposes of s59(1)(c) of the Arbitration Act 1996, and therefore recoverable from Essar. The case was ground breaking for the litigation funding industry.

As well as benefits relating to resourcing, arbitration funding can also have substantial strategic benefits and change the dynamic of a dispute. For example, a funded claimant will often be able to achieve a better settlement outcome more quickly than an unfunded claimant. This is principally because the defendant, on becoming aware of the claimant's funding, will appreciate that the tactic of depleting a claimant's resources to stifle a claim would likely fail. A funded claimant is also less likely to feel any financial pressure to accept a low settlement offer. Further, the support of a sophisticated professional funder signals to a tribunal and the defendant that an objective third-party, with substantial expertise and experience in disputes, is willing to risk its own capital on the merits of the underlying claim and the prospects of making a recovery. Although the conduct and control of a funded claim rests firmly in the hands of the claimant (and its lawyers), a funder – which will often be staffed by expert lawyers with decades of international law firm experience – can also be a valuable resource to the claimant team throughout the life of the claim. For example, a third-party funder often assists the claimant's legal team with key strategic decisions and can attend arbitrations or other settlement discussions, which often helps the claimant to demonstrate its financial strength.

WHAT DO THE INSTITUTIONS SAY?

Where arbitral institutions or other relevant bodies have sought to codify rules or provide guidance in relation to funding, it has usually been in respect of the disclosure of third-party funding arrangements, in order to avoid potential conflicts of interest and to provide parties with guidance in relation to confidentiality and privilege.

One of the first bodies to address third-party funding arrangements was the International Bar Association (IBA). In 2014 it published guidelines in relation to conflicts of interest in international arbitration, which state that the parties in the arbitration have a duty to disclose any relationship, direct or indirect, between the arbitrator and the party. The 'party' for these purposes includes persons or entities having a direct economic interest in the award to be rendered in the arbitration, such as an entity providing funding for the arbitration, or having a duty to indemnify a party for the award, whether under an insurance policy or otherwise. The International Chamber of Commerce (ICC), the Singapore International Arbitration Centre (SIAC), the Hong Kong International Arbitration Centre (HKIAC), and the Center for Arbitration and Mediation of the Chamber of Commerce Brazil-Canada (CAM-CCBC) have all provided similar guidance.

In April 2018, the International Council for Commercial Arbitration (ICCA), in partnership with Queen Mary University of London, published its fourth report in relation to third-party funding in international arbitration. The report outlines a number of principles in relation to third-party funding, including in respect of disclosure and conflicts of interest, privilege and professional secrecy, allocation of costs in final awards and security for costs.

In relation to privilege and confidentiality, the report notes that 'securing funding necessarily requires the sharing of confidential, privileged and, on occasion, highly sensitive information with prospective funders. Ensuring the protection of that confidential information and that any existing privilege is not lost are important

issues that claim holders and their advisors must consider before seeking funding'. In particular, the principles expressly state that while existence of funding and the identity of a third-party funder is not subject to any legal privilege, the specific provisions of a funding agreement may be subject to confidentiality obligations as between the parties, and may include information that is subject to legal privilege. As a consequence, production of such provisions should only be ordered in exceptional circumstances.

More recently, the International Centre for Settlement of Investment Disputes (ICSID) has proposed to amend its rules to include express provisions concerning a tribunal's consideration of third-party funding agreements when determining if security for costs should be ordered against a party. The proposed amendments also contemplate the requirement of parties to disclose the existence and name of any third-party funders. The current proposal makes clear that there is no right to further information or disclosure of the agreement itself under the proposed rule. ICSID notes that irrespective of whether the rule comes into force, to the extent that a third-party funding agreement is relevant to an issue in dispute, a tribunal has the power to order production of the agreement.

GLOBAL DIFFERENCES

How does the permissibility of third-party funding in arbitration differ around the world? Commercial third-party funding as we know it today has its origins in Australia, where it first came to prominence, before migrating to the UK and the US. In these more well-established markets, litigation and arbitration funding has thrived and become a multibillion-dollar industry. Third-party funding is allowed in most major arbitration centres around the world including London, New York and Paris.

In recent times, the use of third-party funding in other jurisdictions has become more common. In Switzerland, third-party funding is allowed, and Geneva remains a major arbitration centre in Europe. In Singapore and Hong Kong, legislation has been introduced that expressly permits the use of third-party funding in international arbitration. In Singapore, the Civil Law Amendment Act and the Civil Law (Third Party Funding) Regulations 2017 allow third-party funding in respect of international arbitration and associated proceedings, including the enforcement of arbitral awards. In Hong Kong, the Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Bill 2016, amended the Arbitration Ordinance which in effect provides that the doctrines of champerty and maintenance no longer apply to third-party funding of arbitration and related court or mediation proceedings. While in Singapore, the legality of third-party funding was limited to *international* arbitration, no such limitation applies in Hong Kong, where third-party funding is allowed in both domestic and international arbitration. In Latin America, broadly speaking, third-party funding is not prohibited in various jurisdictions. In Brazil for example, while third-party funding is still relatively novel when compared with other jurisdictions, the concept is becoming more common. In response to this, Brazil's leading

Continued on page 16

Continued from page 15
arbitration centre the CAM-CCBC, became the first arbitration centre in Latin America to issue guidelines in relation to the disclosure of funding agreements.

One of the more notable jurisdictional exceptions to the acceptance of third-party funding can be found in Ireland. The Supreme Court in *Persona Digital Telephony Ltd v the Minister for Public Enterprise* [2017] IESC 27 has ruled that the common law prohibitions on champerty and maintenance remain in force within the jurisdiction, thereby restricting the availability of third-party funding. While decisions of the Supreme Court in Ireland have not directly dealt with admissibility in international arbitration, the approach adopted by the court means that if the arbitration is seated in Ireland, the permissibility of third-party funding is an important consideration, when at the very least an arbitral award might need to be enforced by the court.

In considering whether third-party funding is permissible in any particular international arbitration, it may be necessary for a practitioner to consider the law of multiple relevant jurisdictions, for example the applicable arbitration rules, the law of the jurisdiction where the arbitration is seated, the governing law of the jurisdiction in which an award will be enforced, and potentially the law of the parties' counsels' home jurisdiction.

OBTAINING FUNDING

There are a number of factors a funder will look at when assessing whether they should finance a party in an arbitration. First, they will look for cases where the merits in respect of liability, causation and quantum are strong. Second, the claimant needs to show they have suffered sufficiently high provable damages in order to make the claim economically viable to be pursued with the help of funding. A funder will usually look for a ratio of 10:1 between the quantum and the funding requirement. For example, if the funding sought is £1m, the realistic provable damages should be at least £10m, otherwise the funder runs the risk of not obtaining a return on the investment and the claimant runs the risk of not recovering a satisfactory proportion of a settlement or arbitral award.

Third, it's vital that the defendant has the financial strength to meet the claim. It will be necessary to show that in the event the arbitration is successful and an award of damages is ordered by the tribunal, the defendant has sufficient assets in a New York Convention state that will be available to satisfy that award. Fourth, the claimant must also have a credible strategy as to where and how a judgment or award against the defendant will be enforced. In this regard, the seat of the arbitration will often be important. Additional important matters the funder will consider include issues in relation to whether the lawyers acting for the party seeking funding are willing to share some of the risk by deferring a portion of their fees, the likely length of proceedings, and the prospects of an early settlement.

Many funders will consider a range of different types of funding relating to arbitration. They may consider agreements to fund single arbitrations or to fund a portfolio, where the investment and return are spread across a number of different arbitrations. In addition, many funders will consider providing finance solutions in late stages of the arbitration process. A successful arbitral award is often not the end of the arbitration process: rather, it can be a staging post along the way to successful recovery. With annulment or other types of appeal process common, contentious and expensive enforcement proceedings are often required. Funders will consider providing funding for claimants who have obtained a successful arbitral award but who require additional support to get through the annulment and / or enforcement stages to ultimate recovery. This type of funding provides claimants with the certainty of access to an immediate cash facility upon a successful award, while taking on some of the risk of potential annulment and / or enforcement proceedings.

Another type of funding that may be available during the arbitration is funding for the upfront fees payable to arbitral institutions, and the deposit for the tribunal's costs. These are usually shared by the parties, and can be significant. Where the respondents fail to pay their share, claimants are forced to pay. Seeking third-party funding for this unexpected liability may be prudent; and as can be seen in *Essar v Norscot*, where the respondent's conduct in such circumstances is demonstrably unreasonable, the claimant may have a good argument that the respondent should be held liable for these third-party funding costs. There may also be scope for claimants to monetise arbitral awards before the respondent has satisfied the award. Cashflow following lengthy arbitrations can become a major issue for law firms and claimants alike, as they face further delays in the realisation of any award. Funders are able to relieve the pressure on cashflow through various financing solutions, such as structured finance arrangements for payment of compensation, or capital funding for business and other expenses not necessarily related to the dispute.

> Third-party funding allows claimants an avenue to justice who may otherwise not be able to bring their claim

CONCLUSION

Third-party funding is a valuable option that parties involved in arbitration should explore. It allows claimants an avenue to justice who may otherwise not be able to bring their claim because of financial constraints. It also has significant strategic benefits, and is a valuable option for companies that have meritorious claims but want to share the costs risk involved with pursuing those claims, and free up resources to be used elsewhere.

When considering whether third-party funding is appropriate in international arbitration, practitioners should consider any jurisdictional constraints of using funding, as well as issues of privilege, disclosure of conflicts and security for costs that may arise, and advise their clients accordingly. Practitioners and claimants alike should also consider the reputation of the funder they intend to transact with, and be careful to choose a funder with a proven track-record that has the ability to meets its obligations under the terms of any funding agreement.

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