

Discussion paper relating to the Proposal for Amendment of ICSID Rules on the provisions relating to Third-Party Funding and to Security for Costs

Scope of work

This discussion paper (“**Discussion Paper**”) is made by the Centro Studi TPF - Third Party Funding (“**TPF Study Centre**”) with legal offices in Milan, Italy.

The Discussion Paper is based on the Proposal for Amendment of ICSID Rules (the “**Draft**”) as provided by ICSID on 3 August 2018 through its website for the purpose of a public consultation on possible future amendments to its Rules.

The Discussion Paper is intended to encompass the proposed amendments relating to both the ICSID Arbitration Rules and the Additional Facility Rules.

In particular, this Discussion Paper involves two key topics:

- A) Disclosure of Third-Party Funding (Art. 21, page 31 of the Draft; Art. 32, page 109 of the Draft);
- B) Security for Costs (Art. 51, page 48 of the Draft; Art. 60, page 125 of the Draft).

TOPIC A: Disclosure of Third-Party Funding (Rule 21 - ICSID Arbitration Rules; Rule 32 Additional Facility Arbitration Rules)

The relevant provisions of the Draft on Third-Party Funding (“**TPF**”) reads as follows:

Disclosure of Third-Party Funding:
(1) “Third-Party funding” is the provision of funds or other material support for the pursuit or defense of a proceeding, by a natural or juridical person that is not a party to the dispute (“Third-Party Funder”), to a party to the proceeding, an affiliate of that party, or a law firm representing that party. Such funds or material support may be provided:
(a) through a donation or grant; or
(b) in return for a premium or in exchange for remuneration or reimbursement wholly or partially dependent on the outcome of the proceeding.
(2) A party shall file a written notice disclosing that it has Third-Party Funding and the name of the Third-Party Funder. Such notice shall be sent to the Secretariat immediately upon registration of the Request for arbitration, or upon concluding a Third-Party Funding arrangement after registration.
(3) Each party shall have a continuing obligation to disclose any changes to the information referred to in paragraph (2) occurring after the initial disclosure, including termination of the funding arrangement.

The proposed comments to this provision of the Draft touch upon two issues:

a) Duty of disclosure:

Need for clearer guidelines in terms of the meaning of the definition.

As the onus lies on a party to decide whether to disclose an arrangement, it would be helpful for ICSID to provide additional guidance around the meaning of the definition, in particular, sub-clause (b), if it is finally adopted in these terms. This guidance might usefully include discussion as to whether the determinative factor is the substance of the arrangement or a

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matter of form. A situation such as a Third-Party Funder (“**Funder**”) would provide the facility and would only be reimbursed if the party wins the brief.

Need for procedural guidelines

The issue relating to the unclear indication of how the information is handled.

Potential overlooks on the economic consequences due to the duty

○ Access of Justice

This duty may cause the cost of compliance to fatally upsurge, as it forces the parties to disclose in all circumstances and at the very first moment information that may have been disclosed anyway in a near future, that is, upon enforcing an award that has possibly favoured the funded party.

○ Delay

“Guerrilla tactics”, that is tactics used by the opposing party in delaying the situation, it is a highly debated and faced issue in modern arbitration, especially with reference to investment arbitrations. With the establishment of such an overarching duty, these parties will be awarded yet another reason to seek information on the investor, trying to pierce multiple levels of the corporate veil until finding the very individuals backing the investment, as to maximize their procrastinating manoeuvres. The result will, without doubt, be a greater delay in the conclusion of arbitral proceedings.

This would lead to higher expenses and delay in the proceeding, with a massive increase in the cost of an investment which may reach ten times the value of the investment. The market follows a rather clear logic in relation to such mechanisms: increase the risks and the costs, and prices shall follow.

If in the event of breaching this duty, the party and the investor are presumed to be tainted by some irregularity, which may make life easier for a losing respondent seeking to annul the arbitral award.

○ Confidentiality

In many TPF, the relationship between party and Funder is governed by the duty of confidentiality. The reasons why the disclosure of TPF may be necessary include the arbitrators’ impartiality requirement, the potential conflicts of interest, and the transparency, the latter, especially in the investment treaty arbitration. Even if the Funder is not the party to an arbitral dispute, it would still participate to a certain extent in various stages of an arbitration.

Therefore, while regulating TPF may be useful, it is important that the arbitral institution pays attentions to balance the duty of confidentiality between the Funder and the party and the need of protection in many cases, of the respondent. Thus, it is understandable that the ICSID Secretariat who received the information regarding TPF shall decide when, if appropriate, disclose the said information to the parties.

b) Insurance

Is insurance exclusively a private matter?

In many arbitrations, insurance has been regarded exclusively as a private matter, which should not be exposed or disclosed in all cases. This notion has been a tradition in many arbitrations since the 19th century, whereby parties likely being supported by all sorts of insurers.

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Issues of confidentiality

Historically, there was never a call for regulating participation of insurance, due to many shortcomings such as the duty of confidentiality in a policy, exposure on coverage issues and commercial vulnerabilities, and an unfair advantage to a powerful self-insured opponent, such as a state. An institution that imposed such an obligation in its rules could jeopardise the level playing field, which it is one of its duties to secure.

Cases where TPF does not extend to insurance

Certain treaties concerning investment do not extend TPF to insurances.

1. CETA
2. EU-Vietnam FTA
3. EU-Singapore Investment Protection Agreement

Indeed TPF does need to be regulated. Many treaties and arbitration rules have dealt with them, mainly used the definition that targets the modern phenomenon of non-recourse funding provided in return.

It is worth noting that the proposal of ICSID, as outlined in the Working Paper that accompanies the Draft¹ (“**Working Paper**”) intends to define TPF ‘*in a manner similar to the definitions in the above texts*’.

However, it seems the ICSID Secretariat decided to depart from this view, favouring instead some wording proposed by the ICCA-Queen Mary Task Force Report on Third-Party Funding², which purports to bring insurance within a definition of TPF.

Yet, having read in detail of the deliberation of the ICCA-Queen Mary Task Force’s Investment Arbitration Sub-Committee, it seems that the committees of the said Task Force assumed that the TPF was the modern form of non-recourse funding. The said report pointed out political risk insurance but as a ‘point of comparison’ (p. 210) and as an alternative to investment treaty arbitration (p. 211), not as an alternative form, or sub-category, of TPF.

Suggestions for amendments and proposed Third-Party Funding clause

The ICSID Secretariat should consider on the following:

- whether it is proper to go beyond the provisions in recent investment treaties, and beyond the type of TPF discussed by the ICCA-Queen Mary Task Force investment arbitration sub-committee; and
- whether the proposed extension of the definition of Art. 21 of the Draft to insurance, implicit in ‘premium’, might be too broad from what’s concerned.

In light of the above considerations, the TPF clause of the Draft proposed by the TPF Study Centre would read as follows:

¹Proposed Amendment of ICSID Rules - Vol. 3: Working Paper, page 252, available at https://icsid.worldbank.org/en/Documents/Amendments_Vol_3_Complete_WP+Schedules.pdf.

²Available at https://www.arbitration-icca.org/media/10/40280243154551/icca_reports_4_tpf_final_for_print_5_april.pdf.

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Disclosure of Third-Party Funding

(1) “Third-party funding” is the provision of funds or other material support for the pursuit or defense of a proceeding, by a natural or juridical person that is not a party to the dispute (“Third-Party Funder”), to a party to the proceeding, an affiliate of that party, or a law firm representing that party. Such funds or material support may be provided:

(a) through a donation or grant; or

(b) ~~in return for a premium or~~ in exchange for remuneration or reimbursement wholly or partially dependent on the outcome of the proceeding.

(2) A party shall file a written notice disclosing that it has Third-Party Funding and the name of the Third-Party Funder. Such notice shall be sent to the Secretariat immediately upon registration of the Request for arbitration, or upon concluding a Third-Party Funding arrangement after registration. The Secretariat shall analyse whether the information of the Third-Party Funding is necessary to be disclosed to those in the arbitration proceeding.

(3) Each party shall have a continuing obligation to disclose to the Secretariat any changes to the information referred to in paragraph (2) occurring after the initial disclosure, including termination of the funding arrangement.

TOPIC B: Security for Costs (Rule 51 - ICSID Arbitration Rules; Rule 51 - Additional Facility Arbitration Rules)

The relevant provision of the Draft reads as follows:

Security for Costs:

(1) A party may request that the Tribunal order the other party to provide security for the costs of the proceeding and determine the appropriate terms for provision of the security.

(2) The following procedure shall apply:

(a) the request shall specify the circumstances that require security for costs;

(b) the Tribunal shall fix time limits for written or oral submissions, as required, on the request;

(c) if a party requests security for costs before the constitution of the Tribunal, the Secretary-General shall fix time limits for written submissions on the request, so that the Tribunal may consider the request promptly upon its constitution; and

(d) the Tribunal shall issue its decision on the request within 30 days after the latest of: (i) the constitution of the Tribunal; (ii) the last written submission on the request; or (iii) the last oral submission on the request.

(3) In determining whether to order a party to provide security for costs, the Tribunal shall consider the party’s ability to comply with an adverse decision on costs and any other relevant circumstances.

(4) If a party fails to comply with an order for security for costs, the Tribunal may suspend the proceeding until the security is provided. If the proceeding is suspended for more than 90 days, the Tribunal may, after consulting with the parties, order the discontinuance of the proceeding.

(5) A party must promptly disclose any material change in the circumstances upon which the Tribunal ordered security for costs.

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(6) The Tribunal may at any time modify or revoke its order for security for costs, on its own initiative or upon a party's request.

The proposed comment on this provision of the Draft lies on several points.

To begin with, it should be considered that the Working Paper describes the above provision as “*a new, stand-alone rule allowing a Tribunal to order security for costs*”. The applicable test is “*the party's ability to comply with an adverse decision on costs and any other relevant circumstances*”. A failure to comply with an order to provide security would entitle the tribunal to suspend the proceeding for up to 90 days, and thereafter, to discontinue the proceeding after consulting with the parties.

Paragraphs 267 and 530 of Working Paper also refers to this regulation of security for costs as a new rule, and do not address the effect of TPF. Instead, the proposed provision requires the tribunal to consider the respondent's ability to comply with an adverse costs decision and whether a security order is appropriate in light of all the circumstances.

In the aspect of the respondent in investment arbitration, the security for costs is used as a protection to legit claims which will affect the taxpayers' resources.

However, on the other side, a claimant might become financially incapable of accessing justice if it is asked to put up security for costs. With a Funder into the mix, it is more obvious that the claimant has a financial situation of which may be caused a concern. These costs may potentially stifle claims as the Funder may think that the claim will be uneconomic.

The unclear standards as to an award for the security of costs adds more layers to the considerations that any tribunal needs to keep in mind while making an award for security for costs.

As a result, the mere fact of the existence of TPF, without relevant evidence of an inability to comply with an adverse costs decision, will continue to be insufficient to obtain an order for security for costs under the proposed provision as set forth above.

Another interesting case for security for cost is the possibility that TPF creates an imbalance in the arbitration equation, because of the possibility of an “arbitral hit and run”. There were many discussions that a security of cost should be granted to avoid misbalanced.

On the other hand, the existence of TPF coupled with other relevant circumstances may form part of the relevant factual circumstances considered by a tribunal in ordering security for costs. This will be a fact-based determination in each case (e.g. *ScT Oil v Romania*, ICSID case no. ARB/07/13 [2010], where security of costs would be beneficial).

Suggestions for amendments and proposed elimination of Security for Costs clause

Among the possible solution to tackle the undesired downsides of a security for costs provision:

Limited disclosure

The idea has recently been introduced and integrated into Rule 24(1) of its Investment Arbitration Rules by the Singapore International Arbitration Centre³. It provides that the tribunal has additional

³ Investment Arbitration Rules of the Singapore International Arbitration Centre, introduced on 1st January 2017, available at <http://www.siac.org.sg/images/stories/articles/rules/IA/SIAC%20Investment%20Arbitration%20Rules%20-%20Final.pdf>.

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powers to order disclosure of TPF arrangements. Furthermore, it also provides for the tribunal to seek disclosure of the Funder's commitment towards adverse costs liability.

Similar provisions can be found in the Iran-Slovakia BIT, Article 21, which expressly provides for the circumstances in which the tribunal may order security for costs if it considers that there is a reasonable doubt that claimant would be not capable of satisfying a costs award or consider it necessary because of other reasons. Such provisions are a move toward ensuring that the presence of a Funder does not unduly affect a party and its ability to seek security for costs.

It is also essential to ensure that there are safeguards against respondents using disclosure of TPF as a weapon instead of a shield. For instance, it is unnecessary to seek disclosure of all the aspects of the TPF agreement. The liability as to the costs for the Funder should be the focal point for disclosure.

If the Draft rule is enforced as it currently is, there would be different interpretations and views by different tribunals. There must be something more than having the TPF to be required for an order to be made. In order to analyse as such, the party's ability to pay will be weighed with matters of such as the desire to allow reasonable claims to proceed, as well as the counterbalancing wish to protect respondents from incurring substantial irrecoverable costs defending themselves against claims that ultimately fail.

Furthermore, in order to find the correct balance for any particular case, tribunals need not decide the amount of security on an all or nothing basis.

The Garcia Armas approach.

It refers to a case⁴ where the tribunal ordered security for costs (independently of the existence of TPF), to make it express in the order that if the claimant ultimately prevails on its claims, the respondent state will be ordered to reimburse the reasonable expenses incurred by the claimant to post the security ordered.

Art. 21 of the Draft does not stipulate security for costs and the Draft provision on security for costs reads to be giving express authority to the arbitrator to order security for costs, meaning tribunals would not be obliged to apply the legal standard applicable to provisional measures.

Therefore, the Draft rule on security for costs would not affect TPF as such, but requires the tribunal to consider the respondent's ability to comply with an adverse costs decision and whether a security order is appropriate in light of all the circumstances. Hence, it can be inferred that the mere existence of TPF, without relevant evidence of an inability to comply with an adverse costs decision, will continue to be insufficient to obtain an order for security for costs under the proposed provision on security for costs.

On the other hand, the existence of TPF coupled with other relevant circumstances may form part of the relevant factual circumstances considered by a tribunal in ordering security for costs. This will be a fact based determination in each case.

In conclusion, it is the impression of the TPF Study Centre that it would be better off at this juncture to not have an express clause relating to security of costs due to the TPF arrangement but rather leave

⁴ *Manuel Garcia Armas et al. V. Bolivarian Republic of Venezuela*, PCA Case No. 2016-08.

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it to arbitrator. It could be a suggestion to the ICSID Secretariat to rather draft proposed guidelines relating to the security of costs.

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- Stewarts - Matthew Knowles
- Kluwer Arbitration Blog, Ulmika Shawar
- American Society of International Law: Alexander G. Leventhal - The 2018 Proposals for Amendments of the ICSID Rules: ICSID Enters the Era of Trump, Populism, and State Sovereignty
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